STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. S871027C

On October 27, 1987, a Petition for Advisory Opinion was received from Thomas B. Bottiglieri c/o Grant Thornton, 605 Third Avenue, New York, New York 10158.

The issue raised is whether a corporation organized to do business in another state, which is a wholly-owned subsidiary of a corporation qualified to do business in New York State, must collect and remit New York State sales and use taxes on property delivered to destinations within New York State.

Subsidiary, a direct marketer who has no property or other presence in New York and does not solicit sales in the State in any manner, sells tangible personal property to individuals placing telephone orders to out-of-state locations. Subsidiary's New York customers order merchandise through a brochure produced by the parent corporation (Parent), receive the goods via commercial carrier or U.S. mail and make payment directly to Subsidiary.

Parent, a foreign corporation qualified to do business in New York State, sells club memberships, entitling members to purchase discounted merchandise, to individual customers and members of unrelated organizations. Employees of Parent enter the State from time to time to service and solicit memberships. Parent has enlisted a network of over 100 vendors that have agreed to sell their merchandise at discount prices to club members. Subsidiary is one of these vendors.

Parent produces and mails brochures advertising the club vendor's merchandise to the members. Parent will take telephone inquires from club members but will not accept orders; it will merely refer the customer to the supplier. Subsidiary is one of the suppliers.

Resolving this issue requires two determinations: (1) whether sufficient nexus exists between the subsidiary corporation (Subsidiary) and New York State to satisfy the Due Process and Commerce Clauses of the United States Constitution and (2) if sufficient nexus is found, whether Subsidiary meets the definition of "vendor" contained in Tax Law §1101(b)(8).

ISSUE **1** - Nexus

A state can require an out-of-state seller to collect the state's sales or use tax only when there is a sufficient nexus between the seller and the taxing state, as required by the Commerce Clause of the United States Constitution (Art. I, § 8, cl. 3) and the Due Process Clause of the Fourteenth Amendment to the United States Constitution. National Geographic Society v. California Board of Equalization, 430 US 551.

The test to determine whether a particular state exaction violates the Commerce Clause by invading the exclusive authority of Congress to regulate trade between the states, and the test to determine whether a state has complied with the requirements of due process in this area, are similar. National Bellas Hess, Inc. v. Department of Revenue, 386 US 753. "[T]he relevant constitutional test to establish the requisite nexus for requiring an out-of-state seller to collect and pay the use tax is not whether the duty to collect the use tax relates to the seller's activities carried on within the State, but simply whether the facts demonstrate some definite link, some minimum connection, between [the State and] the person it seeks to tax." National Geographic Society v. California Board of Equalization, 430 US at 561.

Activities in a state that have been found to be constitutionally sufficient to establish nexus to require an out-of-state corporation to collect state taxes include the operation of retail stores of the corporation in the state, Nelson v. Sears, Roebuck and Co., 312 US 359; Nelson v. Montgomery Ward, 312 US 373; the presence of traveling salesmen in the state, General Trading Co. v. Tax Commission, 322 US 335; and the presence of independent contractors or agents of the corporation in the state, Scripto, Inc. v. Carson, 362 US 207. In the most recent United States Supreme Court opinion on the issue of nexus for use tax collection purposes, National Geographic Society v. California Board of Equalization, supra, the corporation, National Geographic, operated two offices in California. Although the activities in those offices were unrelated to the corporation's mail order activities, the Court held that it was permissible to impose the administrative burden of collecting use taxes on National Geographic. Since the two California offices, regardless of the nature of their activities, had the advantage of the same services, e.g., fire and police protection, as they would have had had their activities included assistance to the mail order operations that generated the use taxes, there was a definite line between National Geographic and the State of California.

Activities in a state that have been held insufficient to establish the necessary nexus to impose the duty to collect use taxes include mail order sales where delivery of the goods was made from out-of-state by common carrier or United States mail, National Bellas Hess, Inc. v. Illinois, supra, and over the counter sales made in a bordering state to state residents with only occasional deliveries being made into that state, Miller Brothers Co. v. Maryland, 347 US 340. In both these cases, the Court found that the requisite relationship between the state and the out-of-state seller was lacking.

To determine whether there will be sufficient nexus for New York State to impose a requirement to collect use taxes on Subsidiary, it is necessary first to determine whether there will be some relationship or minimum connection between Subsidiary and New York State. Under the facts presented here, Subsidiary will not operate directly in New York State, nor will it have any offices in this state. Its sales will be made by mail with delivery by common carrier or mail. Under the holdings of the National Bellas Hess and Miller Brothers cases cited above, on these facts alone Subsidiary will not be required to collect tax. The question thus becomes whether the existence of a parent doing business in New York State is sufficient to establish nexus for Subsidiary with New York.

As a general rule, corporations are treated as separate legal entities, Rapid Transit Subway Const. Co. v. City of New York, 259 NY 472, and the presence of a parent corporation in one state does not require a finding of presence in that state for its wholly-owned subsidiary. However, under certain circumstances in order to prevent fraud or injustice, the corporate structure will be disregarded and the separate entity rule discarded. Astrocom Electronics, Inc. v. Lafayette Radio Electronics Corp, 63 AD2d 765; Giblin v. Murphy, 97 AD2d 668; Berkey v. Third Ave. Railway Co., 244 NY 84. In Nelson v. Sears, Roebuck and Co., supra, the Supreme Court held that the departmentalization of the corporation's operations (i.e., the mail order and retail stores operations were separately administered) did not preclude the finding of sufficient nexus. In New York, there has been a "steady movement towards holding that in determining whether a corporation has engaged in activities in the state it is immaterial whether these are conducted through a branch or through a subsidiary corporation," Boryk v. de Haviland Aircraft Co., 341 F2d 666, 668. In certain cases, this concept should be applied to corporate reorganizations. It would be unjust to permit a corporation to use a corporate reorganization as a cloak for the evasion of its tax obligations.

The status of the subsidiary as a separate entity should be ignored in situations where the parent so dominates and controls the affairs of the subsidiary that the subsidiary is an instrumentality of the parent. Coastal States Trading, Inc. v. Zenith Nav. SA, 446 F. Supp. 330; Fiur Co. v. Ataka & Co., 71 AD2d 370. In such situations, the subsidiary should be considered to be the alter ego of the parent. See, Van Valkenburgh, Nooger & Neville, Inc. v. Hayden Publishing Co., Inc., 30 NY2d 34.

Indicia such as common officers and directors, common offices and telephone numbers between corporate entities are relevant but are not sufficient by themselves to show that one corporation is the alter ego of another. Consideration must also be given to factors such as the degree of overlap of personnel, the amount of business discretion displayed by the corporations, whether the entities operate independently of each other, whether the parent corporation owns all or most of the stock of the subsidiary and whether the parent corporation causes the incorporation of the subsidiary. United States Barite Corp. v. M. V. Haris, 534 F. Supp. 328; Ioviero v. CIGA Hotels, Inc., 101 AD2d 852; Lincoln Center v. State Commission, 113 Misc. 2d 329; Worldwide Carriers, Ltd. v. Aris Steamship Co., 301 F Supp 64. Also significant is whether the corporations trade under their own names and whether they hold themselves out to the public as separate and distinct businesses. Mangan v. Terminal Transportation System, Inc., 247 AD 853; Matter of Sbarro Holding, Inc., 111 Misc. 2d 910, aff'd 91 AD2d 613; Matter of Typhoon Industries, Inc., 6 BR 886; see, also, Plainview Realty v. Board of Managers, 86 Misc. 2d 515; Henn and Alexander, Laws of Corporations and Other Business Enterprises 3d Ed. (1983), pp. 354-356.

If the affairs of the subsidiary or affiliated corporation are so dominated and controlled by its parent or affiliate that the dominated and controlled corporation is the alter ego of the other, then the nexus of one with New York State for tax jurisdiction purposes will provide sufficient nexus with New York State for the other. CIT Fin. Services Consumer Discount Co. v. Director, Div. of Taxation, supra; Minnesota Tribune Co. v. Commissioner of Taxation, 37 NW2d

737; Franklin Mint Corp. v. Tully, 94 AD2d 877, aff'd, 61NY2d 980. (Other cases supporting a finding of nexus premised on a parent/subsidiary relationship include Aldens, Inc. v. Tully, 49 NY2d 525; Reader's Digest Association, Inc. v. Mahin, 44 Ill. 2d 354, 255 NE2d 458, appeal dismissed, 399 US 919; Appeal of Dresser Industries, Inc., California State Board of Equalization, CCH 400-485. See Barber, "Piercing the Corporate Veil," 17 Willamette L. Rev. 371, 397.)

In presenting the hypothetical issue, Petitioner asserts that Subsidiary operates independently from the Parent and that both entities hold themselves out as separate and distinct business enterprises. Petitioner emphasizes that Parent does not exert domination and control over Subsidiary, but fails to state for what purpose it caused the incorporation. However, the facts emerge that Subsidiary, a direct marketer, fills telephone orders from New York customers who became aware of its product through a brochure distributed by the Parent to New York club members.

Thus, Subsidiary sells tangible personal property to New York destinations but disclaims nexus because it has no presence in the State, while the Parent, although it has employees entering the state for service and solicitation, appears to lack nexus for sales tax purposes because it makes no sales in the State. Were the soliciting and selling activities conducted by a single entity nexus would be established between it and New York State Tax Law § 1101(b)(8)(i)(C), infra. Allowing the separate entity rule here would obviously produce inequitable consequences.

Accordingly, the creation of Subsidiary as a separate corporate entity may not preclude the finding of sufficient nexus unless valid reasons for corporate reorganization - other than the separation of promotion and marketing activities - can be demonstrated.

ISSUE 2 - Status as a Vendor

In addition to establishing the constitutionally required nexus with New York, in order to compel a corporation to collect New York State tax, it must also be determined that such corporation is subject to the provisions of the New York State Sales and Use Tax Law. Section 1131 of the Tax Law requires that every vendor of tangible personal property or services must collect the sales and use taxes imposed under Article 28. Tax Law § 1131(1).The term "vendor" is defined under section 1101(b)(8) to include among others

> (A) A person making sales of tangible personal property or services, the receipts from which are taxed by this article;
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> * * *
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> (C) A person who solicits business either by employees, independent contractors, agents or other representatives or by distribution of catalogs or other advertising matter and by reason thereof makes sales to persons within the state of tangible personal property or services, the use of which is taxed by this article; Tax Law, §1101(b)(8)(i)(A) and (C).

The term person includes a corporation or combination of corporations. Tax Law § 1101 (a).

Pursuant to New York State Sales and Use Tax Regulations a person is deemed to be soliciting business if he has employees, salesmen, independent contractors, promotion men, missionary men, service representatives or agents soliciting potential customers in New York or if he distributes catalogs or advertising material in any manner in the State. 20 NYCRR 526.10(d).

Every vendor has certain obligations with respect to registration, collection of tax from customers, filing of returns and payment of tax. 20 NYCRR 526.10(b). A person outside of this State making sales to persons within the State, who solicits the sales in New York is required to collect the sales tax on tangible property delivered in New York. 20 NYCRR 526.10(e)(1).

Every person operating a club or similar merchandising plan, or operating as an independent contractor representing a particular supplier selling tangible personal property is a vendor for sales tax purposes and must collect tax on merchandise sold by him. The person supplying the merchandise is also deemed to be a vendor; both the representative and his supplier are jointly responsible for discharging the obligations of a vendor listed in subdivision (b) of Regulation Section 526.10. 20 NYCRR 526.10(f)(1) and (2).

If Parent and Subsidiary fall within the latter provisions, which clearly outline their status as co-vendors under the Tax Law, corporate structure is immaterial.

However, the facts presented in the Petition do not reveal for what purpose subsidiary was incorporated nor do they state whether Parent is registered as a vendor with the New York State Sales Tax Bureau. Nevertheless, it is apparent that Subsidiary's sales are not separate and distinct from Parent's promotional activities. In fact, the related corporations complement each other in performing the function which define a vendor in Tax Law § 1101(b)(8)(i)(C), supra. As the result of that connection, Subsidiary is deemed a vendor and required to collect sales tax on its sales to New York customers.

DATED: March 2, 1988

s/FRANK J. PUCCIA
Director
Technical Services Bureau

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