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

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Sales Tax
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STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. S920601A

On June 1, 1992, a Petition for Advisory Opinion was received from Building Owners and Managers Association of Greater New York, 350 Fifth Avenue, Suite 316, New York, New York 10118 and The Real Estate Board of New York, 12 East 41st Street, New York, New York 10017.

The issue raised by Petitioners, Building Owners and Managers Association of Greater New York and The Real Estate Board of New York, is whether certain workers are employees of the building owner so that amounts paid by the building owner for their compensation are not subject to the sales and use taxes.

Petitioners represent various building owners and managing agents of office buildings in New York. It is common for owners of office buildings in New York to hire independent managing agents to perform various services at the buildings. These services include administering the payroll, supervising employees of the building, collecting rents, handling tenant inquiries and complaints, and similar matters. In return, the agent typically receives an annual fee of an agreed dollar amount, payable monthly.

A managing agent normally gets a flat fee from the building owner. In addition, if the agent also serves as the leasing agent it receives a fee each time a new lease is signed with a new tenant or a lease with an old tenant is renewed. The managing agent does not receive fees with respect to continuing tenants, either as a percentage of rents or otherwise. The agent's fee is not related to the number of employees at a building or to the size of a building's payroll. Although the agent may consider its costs of providing payroll services in setting the flat fee, it is not reimbursed for its costs and it is at risk if it turns out that its expenses in performing services under an agreement with a building owner exceeds its income.

Workers are typically hired by the agent, but on behalf of the owner. The owner, however, approves prescribed work rules and practices, subject to, and within the limitations of, applicable collective bargaining agreements and labor laws. The owner determines the number of employees, the hours that they will work, and the shifts. In the case of union employees, compensation levels are prescribed by the collective bargaining agreement, but the owner has the right to pay premium rates above the union scale to such employees as the owner chooses. The agent cannot decide to pay amounts in addition to the union scale. In the case of nonunion employees, the owner prescribes the compensation level. The employees work exclusively for the particular owner.

Pursuant to the union contracts, the building owners are liable for covering the building employees under the New York State Disability Benefit Law, the New York State Unemployment Insurance Law and for all other obligations to the employees under the contract. In addition, the building owners are considered employers for tort liability purposes.

When a managing agent contracts with a third party to do work at a building, the contract is always in the name of the agent "as agent for" or "as manager for" the owner. Purchase orders are signed by the agent in the same manner. The agents want to make it clear that the owners, and not the agents, are responsible for payment and for any resulting liabilities.

The agent pays the workers (including all benefits) from, or gets reimbursed from, a special bank account that it maintains for each building that it manages. The rents that the agent collects from tenants in the building are deposited in the account and the owner is asked to replenish the account if the balance in the account is insufficient to pay the operating expenses, including the compensation of the on-site employees. Often, the owner funds the account at the outset before wages are paid. Thus, the workers are paid with the owner's money, not with the agent's.

Typically, three separate accounts are maintained by the agent. The principal account, known as the "operating account", is the one in which rents are deposited and that is funded directly by the owner. When salaries are paid, an amount equal to the payment is transferred from the operating account to another account, known as the "payroll concentration account". Payments of employment taxes are made from this account. Amounts equal to the take-home pay of the workers are transferred to a third account, known as the "payroll account". Checks to the employees are made from the payroll account. The payroll concentration and payroll accounts are nothing more than conduits. The only time that they receive funds is when a payroll is due and the funds that they receive from the operating account are immediately paid out to the taxing authorities and to the workers. If a managing agent operates several different buildings, it will always have a separate operating account for each building and only one payroll concentration account and payroll account through which payments are funneled to the taxing authorities and to the employees of all buildings.

At no time do any funds of the agent pass through the operating account. Some Agents may as a convenience use the payroll accounts to pay their own employees. When they do, the funds flow through the two accounts as conduits on an immediate basis.

In all cases, the operating account indicates that the owner is the beneficial owner of the funds. In some cases, the account is in the name of the owner. In other cases, the account is in the name of the agent "as agent for" or "in trust for" the owner. If a payroll concentration or payroll account is used for several buildings, the account will typically be in the name of the agent without any indication that the funds are held as agent for another. Nevertheless, these accounts are mere conduits and funds that they receive from an operating account maintained for a building are immediately paid out to the tax authorities and to that building's employees.

If the account does not contain sufficient funds when a payroll is due, the agent pays the workers with its own funds and requests immediate reimbursement from the owner. The account is in the name of the agent in trust for the owner, and the owner, and not the agent, is the beneficial owner of the account. The agent's creditors cannot reach the amounts in the account. The agreement between the owner and the agent typically limits the amount that the agent can spend from the

account. The owner can direct the agent to distribute funds in the account to the owner or itself or it can withdraw money from the account at any time. Typically at the end of each month the balance is distributed to the owner, less amounts needed to meet estimated future expenses.

The employee wages are reported on Forms W-2 issued by the agent. The owners and the agents both treat the payments of compensation to the employees for income tax purposes as payments made directly by the owner to the employees. The owners deduct those amounts as compensation to employees. The parties do not treat the payments as if the owners paid a management fee to the agent which then paid compensation to its employees.

The collective bargaining agreements with the unions are negotiated by the Realty Advisory Board, an organization of owners and agents. The agent, on behalf of and as agent for the owner of each building, signs an "assent agreement" in which it agrees to have the Realty Advisory Board represent it in connection with union matters. Union grievances are typically filed against the Realty Advisory Board, which conducts the negotiations. The unions and the National Labor Relations Board regard both the owner and the agent as the party with whom they must deal.

In the case of union employees, the agent does not have the right to transfer workers from one building to another. If the agent of a building resigns or is fired by the owner and the owner hires a new agent, the workers at the building must remain at the building and go on the payroll of the new agent. Neither the agent nor the owner can transfer an employee from one building to another building without the union's consent. Seniority is based on service at the building. If a worker moves to another building, he or she starts at the bottom of the seniority ladder even if he or she is on the payroll of the same agent. Eligibility and participation in union pension plans and other benefits is not affected because these are administered on an industry-wide basis. The agent is generally prohibited by contract or practice from transferring nonunion employees without the owner's consent.

The Standard Management Agreement of the Real Estate Board of New York, Inc. entered into by building owners and agents provides, in part, as follows:

Article I

> Exclusive Agency: Owners hereby appoints Agents as the sole and exclusive renting, sale and management agent of the Owner's property known as ...

Article II

* * *

> Employees: (h) Agent agrees in behalf of Owner to supervise the work of and to hire and discharge employees. Agent agrees to use reasonable care in the hiring of such employees. It is expressly understood and agreed, however, that all employees are in the employ of Owner solely and not in the employ of Agent and that Agent is in no wise liable to employees for their wages and compensation nor to Owner of

others for any act or omission on the part of such employees.

The standard Management Agency Agreement of the Real Estate Board of New York, Inc. entered into by building owners and agents provides, in part, as follows:

> 1. Owner hereby appoints Agent sole agent for the management of (hereinafter) referred to as the "Building" or the "Property"). Agent shall use its best efforts in the management of the Building and due diligence in collecting the rents and other income therefrom.
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> 2. Agent agrees on behalf of Owner to supervise the work of, and to hire and discharge employees of the Building, and agrees to use reasonable care in the hiring of such employees. It is agreed, however, that unless Owner specifically requests otherwise, all employees are in the employ of Owner solely had not in the employ of Agent, and that Agent is in no way liable of any such employees for their wages or compensation nor to Owner or others for any act or omission on the part of such employees.
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> In the event Owner specifically request that Agent employ the employees necessary for the operation an maintenance of the Building, it is agreed that all such employees shall be the employees of the Agent or one of its subsidiaries, as an independent contractor, and not the employees of Owner. All wages, salaries and other compensation paid to such employees including all items payable in respect to the payroll, such as but not limited to, unemployment insurance, social security, workmen's compensation, disability benefits, medical and surgical plans now in existence or hereafter imposed or included in union agreements which Agent may enter into, shall be considered as operating expenses of the Property.

Section 1105(c)(5) of the Tax Law imposes a sales tax on the receipts from every sale, except for resale, of: "[m]aintaining, servicing, or repairing real property, property or land ... . Wages, salaries and other compensation paid by an employer to an employee for performing as an employee the services described in paragraphs (1) through (5) of this subdivision (c) are not receipts subject to the taxes imposed under such subdivision."

Section 527.7 of the Sales and Use Tax Regulations states, in part:

> Maintaining, servicing or repairing real property. [Tax Law § 1105(c)(5)]
>
> (c) Exclusions.
>
> * * *

2) Where repair and maintenances service are rendered by an employee for his employer, the wages, salaries and other compensation paid to the employee are not receipts subject to tax for the performance of such services. (emphasis added)

In determining whether a relationship of master and servant or employer and employee exists, the courts have consistently ruled that the determining element is the employer's right to direct and control the work of the employee.

In Brown v. St. Vincent's Hospital, 222 AD 402, the Court stated, "... [t]he relation of master and servant, or of employer and employee, is created by contract, express or implied. (McNamara v. Leipzig, 227 N.Y. 291, 294.) In determining whether or not such relation exists where the question of the contract is obscure, certain tests may be applied as bearing on the relationship. Primarily the test is the right of the employer to control and direct the work of the employee.(Baldwin v. Abraham, 57 App. Div. 67, 74; affd., 171 N.Y. 677; Meredosia Levee & Dr. Dist. v Industrial Comm; 285 ILL. 68.) Other tests, sometimes of value but not fully determinative of the question, are the payment of wages, and the right to hire and discharge.(Braxton v. Mendelson, 233 N.Y. 122, 124.)"

In Hardy v. Murphy, 29 AD2d 1038, the Court stated" ... In determining the issue of employer-employee relationship, it has been held that it is a question of control in the absence of which there can be no finding of employment. (Matter of Morton, 284 N.Y. 167, People ex rel Feinberg v. Chapman, 274 App. Div. 715.)"

In Greene v. Gallman, 39 AD2d 270, the Court stated" ... It is the degree of control and direction exercised by the employer that is determinative of whether or not the taxpayer is an employee. (Matter of Frishman v. New York State Tax Comm., 33 AD2d 1071, mot. for lv. to app. den. 27 NY2d 483; Matter of Hardy v. Murphy, 29 AD2d 1038; Matter of Britton v. State Tax Comm., 22 AD2d 987, • affd, 19 NY2d 613.)"

In Albany College of Pharmacy v. Ross, 404 N.Y.S.2d 779, the Court stated" ... [I]t is said that at common law there are four elements which are considered upon the question whether the relationship of master and servant exists--namely, the selection and engagement of the servant, the payment of wages, the power of dismissal and the power of control of the servant's conduct... ' (53 Am. 3ur. 2d, S2; see, also, Matter of Pelow v. Sork Enterprises, 39 AD2d 494, 496, 337 N.Y.S.2d 218. 220 affd. 33 N.Y.2d 944, 353 N.Y.S.2d 729, 309 N.E.2d 130), but of all the distinguishing elements, it is the power of control which is conclusive (Matter of Liberman v. Gallman, 53 AD2d 766, 767, 384 NYS2d 252, 253 revd on other grounds 41 N.Y.2d 774, 396 N.S.2d 159, 364 N.E.2d 823; Matter of Hardy v. Murphy, 29 A.D.2d 1038, 1039, 289 N.Y.S.2d 694)."

In Currier v. International Magazine Co., Inc., 256 NY 106 (1931), the Court held that managing agents of an apartment building were not liable for an accident which resulted from a handyman's negligent operation of the building's elevator. The Court opined that the agents' liability depended on whether Greig was their employee or the owner's. The agents were paid a commission on apartment rentals in return for attending to repairs and tenants, collecting rents, purchasing

supplies, and discharging and paying building employees. The Court concluded that since the agents had not hired the building employees for their own benefit but, rather, that they had acted on behalf of the owner. The Court found that "[a]ll of [the agents'] efforts were expended in behalf of [the building] owner and Greig was the servant of [the owner] and not of the agents." Id. at 110. The agents were held not to be liable for the consequences of Greig's acts.

Internal Revenue Ruling 70-267, 1970-1 C.B.205 provides, in part, as follows:

> The question presented is whether the owner of improved real estate or R company, the managing agent for the owner, is the employer of the individuals engaged in the operation of the property, for purposes of the Federal Insurance Contributions Act, the Federal Unemployment Tax Act, and the Collection of Income Tax at Source on Wages (chapters 21, 23,and 24, respectively, subtitle C, Internal Revenue Code of 1954).
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> R company manages improved real estate for the owner thereof under an agency contract. Under the contract R, as agent of the owner, employs, pays, and discharges building managers, janitors, maids, and other help. R supervises these employees but it is not responsible for the payment of their wages except from the funds of the owner in its possession that are deposited in a special bank account in the owner's name. The owner's funds are not commingled with the funds of R.
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> For the purposes of the Federal employment taxes the usual common law rules ordinarily apply in determining whether the employer-employee relationship exists and, if so, who is the employer. Guides for determining the employer-employee relationship are found in three substantially similar sections of the Employment Tax Regulations, namely, sections 31.3121(d)--1(c), 31.3306(i)--1, and 31.3401(c)--1.
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> Although R hires, pays, discharges, and otherwise controls and directs the services of the individuals employed in the operation of the owner's property, the individuals are not employees of R under the usual common law rules. R is merely the agent and, as such, is authorized by the owner to employ individuals for and on his behalf. Under the stated facts it is the owner, acting through R, who exercises or has the right to exercise over the individuals in the performance of their services the control necessary under the usual common law rules to establish the relationship of employer and employee. Accordingly, the individuals so employed are employees of the owner and not of R company for purposes of the Federal Insurance Contributions Act and the Federal Unemployment Tax Act.
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> This conclusion is also applicable for purposes of the Collection of Income Tax at Source on Wages.

In the instant case, while the workers are typically hired by agent and sometimes placed on the payroll of the agent or its subsidiary, the owner approves the prescribed work rules and practices

for the workers, in cooperation with the collective bargaining agreements and labor laws, determines the number of employees, the work hours and shifts, the compensation levels for nonunion employees and the amount of premium rates above the union scale for union workers to be paid to such workers. Moreover, pursuant to the agreements between the owners and agents it is expressly provided that the employees are in the employ of the owners solely and not in the employ of the agent. In addition, while the agent sometimes pays the workers and issues W-2 forms in its own name as the employer, the owners reimburse the agent for all payroll expenses incurred and, in most cases, the payroll checks are drawn on a special payroll account in the name of the agent in trust for the owner. Moreover, the building owners are liable for covering the employees under the New York State Disability Benefit Law, the New York State Unemployment Insurance Law and for tort liability purposes. Therefore, pursuant to Section 1105(c)(5) of the Tax Law, Section 527.7 of the Sales and Use Tax Regulations, the above noted court decisions and Revenue Ruling 70-267, supra, since the workers are employees of the owners, the wages, salaries and other compensation paid to the employees for the performance of their services are not receipts subject to sales tax.

It is noted that in instances other than those described above, where the owner specifically requests the agent to employ the employees necessary for the operation and maintenance of the building and it is agreed that such employees are solely the employees of the agent, that pursuant to Section 1105(c)(5) of the Tax Law, Section 527.7 of the Sales and Use Tax Regulations and the above noted court decisions the receipts for such services are subject to sales tax.

DATED: October 4, 1993

/s/
PAUL B. COBURN
Deputy Director
Taxpayer Services Division

NOTE: The opinions expressed in Advisory 0pinions are limited to the facts set forth therein.