STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
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July 15, 1996

Mr. M--- B---
Manager, State and Local Tax Practice
--- --- LLP
--- --- Street
--- ---, CA XXXXX

Re: Unidentified Taxpayer

Dear Mr. B---:

This is in response to your letter received by us on April 30, 1996 regarding the application of sales and use tax to the activities of your client.

I note that the only basis for the Board to relieve a person of otherwise properly due taxes is pursuant to the provisions of Revenue and Taxation Code section 6596. To come within the provisions of that section, the taxpayer must have reasonably relied on the Board's written advice which was in response to a written request for advice that disclosed all relevant facts, including the identity of the taxpayer. Since your client is not identified, this opinion does not come within the provisions of section 6596.

You state:

> "Our client ('The Company') is headquartered in Nevada. The company is in the business of wholesaling and retailing active apparel. The company has no locations in California.
>
> "The company is comprised of two separate divisions. The first is the wholesale division and the second is the retail, mail-order division. The divisions keep separate sets of books and records. The executive management is the same for both divisions, although each division has [its] own operations management team.
>
> "The sales for the wholesale business are conducted through independent contractors who periodically solicit sales from California distributors. The company has no direct control over the independent contractors. The independent contractors are authorized to solicit sales from only distributors. They are not allowed to solicit sales from individuals, the end user of the products. The independent contractors are not employees of the Company, but receive a commission on sales....The independent representatives are able to represent

> numerous business entities at their own discretion....The independent contractor forwards sales orders to the Company's headquarters located in Nevada for acceptance or rejection. All credit is approved and granted by the Company. The Company does not own or lease any land, buildings or tangible personal property within California. All the products are shipped from Nevada to California via common carrier.
>
> "The sales for the retail business are transacted through mail-order solicitations from catalogs and direct mail advertising brochures. The products are distributed from the Nevada warehouse by common carrier to the California customers. The independent contractors for the wholesale division do not solicit orders for the mail-order division nor do they solicit orders from end users of the active apparel."

You ask whether the analysis would be different if, rather than the company's being comprised of two separate divisions, it were instead comprised of two subsidiaries that are separate legal entities, with one subsidiary making strictly wholesale sales, and the other making only retail, mail-order sales.

Retail sales of tangible personal property in California are subject to sales tax, measured by gross receipts, unless specifically exempt from taxation by statute. (Rev. & Tax. Code § 6051.) When sales tax does not apply, such as when sales take place outside of California, the use tax, measured by the sales price of the property sold, applies to the use of property purchased from a retailer for storage, use, or other consumption in California unless the use is specifically exempt from taxation by statute. (Rev. & Tax. Code §§ 6201, 6401, Reg. 1620.) Although the purchaser is liable for the use tax, a retailer engaged in business in this state is required to collect that tax from the purchaser and to pay that tax to this state. (Rev. & Tax. Code §§ 6202, 6203, 6204.)

From the facts you have provided, it appears that the sales take place outside of California; therefore, the use tax, rather than the sales tax, is applicable. You state that your client does not have an office or other place of business in California, but you indicate that independent contractors enter this state for the purpose of soliciting sales from California distributors. You state your belief that your client should not be considered engaged in business in this state for the following reasons: because the representatives who enter this state solicit sales for resale only and not retail sales; because the representatives are not employees, but are instead independent contractors who represent other businesses in addition to representing your client; and because the company has no "direct control" over the independent contractors. You also state your belief that even if we do consider the wholesale division or subsidiary to be engaged in business in this state, the retail division or subsidiary should not be considered engaged in business in California because the retail division or subsidiary is "completely autonomous from" the wholesale division or subsidiary.

Revenue and Taxation Code section 6203 defines when a retailer is engaged in business in this state. As relevant to your client, subdivision (b) of section 6203 defines a retailer engaged

in business in this state to include "any retailer having any representative, agent, salesperson, canvasser, independent contractor, or solicitor operating in this state under the authority of the retailer or its subsidiary for the purpose of selling, delivering, installing, assembling, or the taking of orders for any tangible personal property."

You state that the company is "in the business of wholesaling and retailing active apparel." This means that your client, which is comprised of retail and wholesale divisions, is a seller making retail sales of tangible personal property; therefore, your client is a retailer for purposes of the Sales and Use Tax Law. (Rev. & Tax. Code §§ 6014, 6015.) Your client is a retailer without regard to whether one of its divisions sells only for resale. (Business Taxes Law Guide Annotation 220.0220 (10/26/64).)

You explain that the independent contractors are not employees of your client, and that they are also able to represent companies other than your client. Please note that a retailer is engaged in business in this state under subdivision (b) of section 6203 if that retailer has any representative or agent in this state for an activity related to sales of tangible personal property. Section 6203(b) is consistent with the constitutional guidelines set forth by the United States Supreme Court in cases involving a state's taxing authority over out-of-state retailers.

In *Quill Corporation v. North Dakota* (1992) 504 U.S. 298, which you cite in your letter, a retailer outside North Dakota challenged that state's amendment of its use tax collection statute which, as amended, reached the Quill Corporation. Quill maintained no locations or employees in North Dakota. Quill did, however, solicit business in that state through catalogs and flyers, advertisements in national periodicals, and by telephone. All property sold to consumers in North Dakota was delivered to them by mail or common carrier.

The Court in *Quill* concluded that the rule for imposing a use tax collection duty on an out-of-state retailer would continue to be the same bright line test enunciated in *National Bellas Hess, Inc. v. Department of Revenue of Illinois* (1967) 386 U.S. 753. (*Quill, supra*, at p. 108.) That test requires some physical presence in the taxing state before a retailer may be required to collect a state's use tax. This means that in the absence of specific Congressional legislation to the contrary, a state may not require an out-of-state retailer to collect use tax from its customers inside that state if that retailer has no physical presence within that state.

The finding of a physical presence is, however, easily met. In a case in which the retailer's only physical presence in a state was through the use of jobbers rather than employees to sell tangible personal property, the Supreme Court held that it was without constitutional significance that the retailer's salespeople were not employees of that retailer. (*Scripto, Inc. v. Carson* (1960) 362 U.S. 207.) In *Tyler Pipe Industries, Inc. v. Washington Department of Revenue* (1987) 483 U.S. 232, the Supreme Court held that the showing of a retailer's physical presence in a state cannot be defeated by the argument that the representative was properly characterized as an independent contractor. Therefore, it is not necessary for an individual to be your client's employee, or to solicit sales exclusively for your client, in order for that individual to operate as your client's representative within the meaning of section 6203(b). (See BTLG Annots. 220.0100 (11/30/64), 220.0230 (4/10/70).)

You indicate your belief that your client's activities should not constitute your client's having authority over its independent representatives. The phrase "under the authority of" in section 6203(b) refers to any relationship pursuant to which any power whatsoever is delegated by the out-of-state retailer to its California representative. (See *Scholastic Book Clubs, Inc. v. State Board of Equalization* (1989) 207 Cal.App.3d 734; BTLG Ann. 220.0020 (8/29/58.) Your client is a retailer with sales representatives who are physically located in this state when they solicit sales of tangible personal property under power delegated to them by one of the divisions of your client; therefore, your client is a retailer engaged in business in this state under Revenue and Taxation Code section 6203(b). As such, your client must collect the applicable use tax from all of its California purchasers and pay that tax to this state, without regard to whether the purchases are made through one of your client's California representatives, or entirely by mail or telephone, and without regard to which corporate division makes the sale. (Rev. & Tax. Code § 6005.)

It is not clear from the information you have provided whether, if the divisions were instead subsidiaries, they would be considered legal entities completely separate from one another. If the retail division were incorporated as, and recognized as, a corporate entity separate from the wholesale division, and if all required formalities in the incorporation procedure were followed, the retail entity would be considered engaged in business in this state only if the activities of the retail entity itself brought it within one of the relevant subdivisions of section 6203. For example, if the wholesale entity (or its independent contractors or other representatives in California) acted as the retail corporation's agents or representatives in California, the retail corporation would be required to collect use tax on all of its sales to California consumers.

You ask whether your client must register with this state. As discussed above, based on the facts you have provided, our understanding is that your client is currently engaged in business in this state under section 6203(b). As a retailer engaged in business in this state, your client must immediately register with this Board. (Rev. & Tax. Code § 6226.) For information regarding registering with this Board, please contact our Out-of-State District Office at 450 N Street, P.O. Box 188268, Sacramento, CA 95818-0268, (916) 322-2010.

If you have further questions, please feel free to write again.

Sincerely,

Kelly W. Ching
Tax Counsel

KWC:cl

cc: San Francisco District Administrator