STATE OF CALIFORNIA
BOARD OF EQUALIZATION **220.0162**

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| In the Matter of the Petition for Redetermination Under the Sales and Use Tax Law | ) | DECISION AND RECOMMENDATION OF HEARING OFFICER |
| R---, INC. dba A--- T--- M--- CO.) | ) | Account SN -- XX XXXXXX |
| Petitioner | ) | |

The above-entitled matter came on regularly for hearing on Thursday, August 10, 1972 in West Los Angeles, California.

Appearing for the petitioner was Mr. R--- S. R---, of the firm of M--- & P---, Attorneys at Law; for the Board none.

Protested Item
(Period 7/1/65 to 12/31/71)

| | 4% | 5% |
|---|---|---|
| Taxable sales not reported | $41,667 | $88,333 |

Petitioner's Contention

The taxpayer is not required to collect use tax on direct mail order sales because it is not engaged in business in California.

Summary of Petition

The taxpayer is a foreign corporation with offices located in --- ---, Iowa.

The taxpayer has entered into a series of agreements with U--- A--- L--- (U---) and possibly others for the sale of --- gifts and souvenirs. The pertinent provisions of the agreements with U--- were summarized in an October 6, 1971, memorandum prepared by Tax Counsel J. K. McManigal as follows:

> "Pursuant to the June 1965 agreement, U--- A--- L--- (U---) granted to R---, Inc., a nonexclusive license to use the registered service mark "U---" on --- bags manufactured, distributed, and sold by R---, Inc.

> Such --- bags were to be available for purchase by U--- or the public, either direct or through wholesalers, distributors, retailers or other merchandising channels, but U--- and its --- agents also had the right to sell or give away directly to U---'s customers --- bags purchased from R---, Inc. (paragraph 1). R---, Inc., agreed, among other things, to provide and maintain adequate stocks of --- bags bearing U---'s service mark at every location where U--- was the sole or major occupant of a --- --- facility and at any other locations where the --- bags were sold at retail. Also, it was to have its representatives make periodic calls at each retail location to provide prominent and proportionately adequate point-of-purchase display of --- bags (paragraph 5).
>
> "Pursuant to the May 1966 agreement, U--- and R---, Inc., established a mail order program to promote the sale of --- bags and other merchandise. R---, Inc., was to maintain an inventory of merchandise described in a catalogue entitled 'U--- A--- L--- T--- G--- and S---', and it was to provide part of that inventory and U--- was to provide the remainder thereof. The price to be paid U--- by R---, Inc., for merchandise supplied by U--- was to be agreed upon but was not to exceed the actual cost thereof to U--- plus 10 percent (paragraph 1). R---, Inc., was to furnish to U--- monthly a written report listing all sales of said merchandise and was to remit to U--- an amount equal to 10 percent of the total gross receipts, that 10 percent being referred to as an advertising allowance (paragraph 2). U---, in order to promote the sale of merchandise to its passengers, was to distribute and maintain an adequate supply of catalogues (paragraph 3), and it had the right to audit the books and accounts of R---, Inc. (paragraph 4). It was specifically provided that nothing therein was to amend, affect, or diminish in any way the June 1965 agreement, and R---, Inc., acknowledged and agreed to its manufacture and sale of certain merchandise was to remain subject to all terms and conditions stated in that prior agreement (paragraph 8).
>
> "The November 1967 agreement established a mail order program to promote the sale of --- bags and other merchandise to members of the --- Club, and it contained provisions comparable to those set forth in the May 1966 agreement."

The taxpayer does not hold a seller's permit or Certificate of Registration to collect use tax. It has consistently refused to allow the board's auditors to examine its books and records or discuss its method of marketing products to California customers. In view of this the Board issued an estimated determination for a sales and use tax deficiency dated April 21, 1972. It is this determination that is the subject matter of this petition.

On August 10, 1972, a preliminary hearing and discussion was held with the taxpayer's attorney. He advised that all items marketed through --- gift shops would have been reported by the gift shop operators under their own respective permits. It was indicated that any direct mail

order sales would have been carried on as a separate business activity unrelated to the gift shop sales. The court's decision in Montgomery Ward & Co. v. State Board of Equalization, 272 Cal.App.2d 273* cert. den., 396 U.S. 1040 [24 L.Ed.2d 684] was cited as authority that the taxpayer's connection or "nexus" with California was not sufficient to require it to collect use tax on direct mail order sales.

*Should be 272 Cal.App.2d 728. SPJ 7/6/00.

It appears that the taxpayer does not have any local employees but that it does have agents who engage in solicitation within the state. In this regard a letter from counsel for the taxpayer, H---, L---, B--- & H--- dated July 22, 1968 (copy in file) provides as follows:

> "We are attorneys for A--- T--- M--- Company, a division of R---, Inc., --- ---, Iowa. This is a manufacturing company in Iowa. It does not have any employees that solicit orders from state to state, including California. However, throughout the country there are manufacturer's representatives who handle a number of lines, including products of A--- T---, who do solicit orders in the various states, including California.

Analysis and Conclusions

If a person fails to make a return, the Board is authorized to estimate his liability and issue a determination for a tax deficiency on the basis of any information which is in the board's possession or may come in its possession. (Cal. Rev. & Tax Code, Sec. 6511.) There is information that the taxpayer is soliciting sales to California residents and that it has refused to make its books and records available for examination. Accordingly the estimated tax deficiency is in accordance with law if the taxpayer is "engaged in business in this state."

What constitutes a retailer engaged in business in this state is set forth in the following quoted provisions of Revenue and Taxation Code Section 6203.

> "'Retailer engaged in business in this state' as used in this and the preceding section means and includes any of the following:
>
> "(a) Any retailer maintaining, occupying, or using, permanently or temporarily, directly or indirectly, or through a subsidiary, or agent, by whatever name called, an office, place of distribution, sales or sample room or place, warehouse or storage place or other place of business.
>
> "(b) Any retailer having any representative, agent, salesman, canvasser or solicitor operating in this state under the authority of the retailer or its subsidiary for the purpose of selling, delivering, or the taking of orders for any tangible personal property.

"(c) As respects a lease, any retailer deriving rentals from a lease of tangible personal property situated in this state."

It can be seen that these definitions are intended to encompass the broadest minimum contacts regarded as sufficient to satisfy the constitutional test of due process and the Commerce Clause provisions of the U--- States Constitution. A requirement that the out-of-state retailer collect use tax on sales to California customers has received judicial sanction in many cases. (See for example Felt & Tarrant Manufacturing Co. v Gallagher, 306 U.S. 62; People v. West Publishing Co., 35 Cal.2d 80.) It is not required that the out-of-state sale be made as a result of local intrastate activities of the retailer. (Nelson v. Montgomery Ward & Co., 312 U.S. 373, 377.) In the case of direct mail order sales the constitutional test is satisfied if the retailer is engaged in local business activity in the taxing jurisdictions even though that activity may be unrelated to the direct mail order sales. (Nelson v. Sears Roebuck & Co., 312 U.S. 359, 365.) Solicitation by independent contractor salesmen has been held to constitute a sufficient local activity requiring the out-of-state retailer to collect the use tax (Scripto v. Carson, 362 U.S. 207).

In the instant case there is evidence that the taxpayer has agreed to provide and maintain inventory at certain locations in California and that "its representatives make periodic calls at each retail location to provide prominent and proportionally adequate point of purchase display of --- bags." Additionally there is evidence that its sales to California customers were promoted by the distribution of catalogues and advertising media by its authorized representative U---. These activities carried on within the State of California on behalf of the taxpayer support a finding that it was engaged in business in this state and satisfy the constitutional requirement of "nexus" or jurisdiction to require the collection of use tax.

Montgomery Ward & Co., v. State Board of Equalization, supra, cited by the taxpayer, is readily distinguishable from the facts of this petition. There all incidents of the sale, including delivery of the merchandise, took place outside California. Indeed the record did not directly show that the purchasers were going to use the property in California. The only local connection with the sale was a California address in the plaintiff's credit files. (See page 740 of opinion.) Thus the court held that the application of the use tax was inherently discriminatory in view of the fact that Nevada and Oregon retailers not maintaining any place of business in California were not required to collect the tax from California customers. Here there is evidence that sales solicitation takes place in California and the property is in fact mailed to the customer in this state. The mere fact that some sales may be completed by means of mail order and direct mailing does not warrant a finding that these sales must be segregated and subjected to a separate constitutional test. They are a part of the business activity conducted by the taxpayer in this state and in view of its local business contacts collection of the use tax is required (Nelson v. Sears Roebuck, 312 U.S. 373; Scripto v. Carson, 362 U.S. 207).

Recommendation

It is recommended that the taxes be redetermined without adjustment. The taxpayer should be afforded a period of thirty (30) days to makes its books and records available for audit examination.

W. E. Burkett, Hearing Officer

9/26/72
Date