STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition of **TRADEARBED, INC.** for Redetermination of a Deficiency or for Refund of Corporation Franchise Tax under Article 9-A of the Tax Law for the Years 1977 through 1981.	:	DECISION

Petitioner, Tradearbed, Inc., 825 Third Avenue, New York, New York 10022, filed an exception to the determination of the Administrative Law Judge issued on September 24, 1987 with respect to its petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the years 1977 through 1981 (File No. 802706). Petitioner appeared by Murphy, Hauser, O'Connor & Quinn, Esqs. (William J. McCann, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Michael J. Glannon, Esq., of counsel).

The petitioner submitted a brief on exception. The Division submitted a brief in opposition. Oral argument, at the request of the petitioner, was heard on July 12, 1988.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUE

Whether the Division of Taxation, in revising petitioner's business allocation percentages, properly recalculated the receipts factor on the basis that petitioner was a selling agent of its parent corporation.

FINDINGS OF FACT

We find the facts as stated in the Administrative Law Judge's determination and such facts are incorporated herein by this reference. Such facts may be summarized as follows.

Petitioner, Tradearbed, Inc., (denominated "TradeARBED" on its invoices and elsewhere) filed corporation franchise tax reports for the years 1977 through 1981, showing entire net income and business allocation percentages as follows:

YEAR	NET INCOME	BUSINESS ALLOCATION PERCENTAGE
1977	$1,321,518.00	41.91994
1978	938,923.00	26.594
1979	1,385,641.00	28.889
1980	780,499.00[1]	32.394
1981	429,893.00	33.158

On August 19, 1985, the Division issued five notices of deficiency to petitioner, asserting corporation franchise tax plus interest as follows:

PERIOD ENDED	TAX	INTEREST
December 31, 1977	$74,372.00	$75,922.00
December 31, 1978	47,811.00	43,718.00
December 31, 1979	69,313.00	56,001.00
December 31, 1980	18,776.00	13,171.00
December 31, 1981	59,462.00	31,653.00

Petitioner was an importer of steel products for resale to customers throughout the United States. Its principal office was in New York City. During the audit period, petitioner was owned by two related European companies, Tradearbed, S. A. and Tradearbed Participants, which were owned in turn by Arbed, Inc. Petitioner bought and sold structural steel, merchant bars for warehouses and steel coils for industry. It purchased the majority of these products from its related companies which owned and operated steel mills in Belgium and Luxembourg.

The asserted deficiencies resulted from a field audit and a consequent recalculation of petitioner's business allocation formula. Petitioner calculated its business receipts factor by including, among other relevant factors, "sales of tangible personal property" (which were made

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[1]Petitioner subsequently filed an amended return and reported an entire net income of $27,749.00.

primarily outside of New York State) and "services performed" (which were performed primarily inside New York State). The Division determined that petitioner was, in fact, a selling agent of its affiliated corporations, and as such it had no sales of tangible personal property of its own. Accordingly, the Division recalculated petitioner's business receipts factor by entirely omitting gross sales from the computation. This resulted in business receipts factors of 95.0575 percent in 1977; 97.5239 percent in 1978; and 100 percent in 1979, 1980 and 1981.

With gross sales omitted from the calculation, petitioner's primary source of business receipts, as shown on its tax reports, was "services performed". The same amounts were referred to on petitioner's financial statements as "Commissions". The fact that petitioner received commission income was a major factor in the Division's determination that petitioner was a selling agent. Other factors were petitioner's practice of maintaining little or no inventory and petitioner's extremely low profit margin, slightly more than one percent. The Division considered the low profit margin to be an indication that petitioner's net income resulted from sales commissions rather than sales of tangible personal property. The following chart illustrates the importance of petitioner's commission income for its overall profits:

YEAR	GROSS PROFITS FROM SALES	COMMISSIONS	NET INCOME
1977	$ 848,571.00	$1,998.702.00	$1,321,518.00
1978	1,219,098.00	1,466,664.00	938,923.00
1979	2,137,864.00	1,590,571.00	1,385,641.00
1980	2,150,384.00	1,346,142.00	780,499.00
1981	2,381,216.00	1,757,870.00	429,893.00

Petitioner's accountant testified that the term "commission", as used by petitioner during the years at issue, actually denoted mill discounts on purchases petitioner made from its suppliers. Invoices established that petitioner received such discounts ranging from 1 to 2.5 percent from both affiliated and unaffiliated steel mills.[2]

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[2]A discount of 1.5 percent on purchases from affiliated steel mills, as shown by petitioner, was the result of an agreement between petitioner and the Internal Revenue Service regarding product pricing stemming from an I.R.S. audit of petitioner several years prior to those in issue

Petitioner's customers were steel fabricators, who bought specific sizes for specific jobs in construction or industry, and steel distributors, who stocked standard length steel for resale. The vast majority of petitioner's purchases were made for specific customers. Petitioner's sales personnel solicited orders and then petitioner negotiated with its supplier steel mills for price and availability of goods. All of petitioner's contracts of sale with its customers provided: "THIS ORDER IS SUBJECT TO OUR MILL'S FINAL ACCEPTANCE". Thus, the customer was aware that it had no contract with petitioner until petitioner's mill accepted the order by agreeing to produce the final product. Petitioner's vice-president testified that petitioner places, at present, approximately 60 percent of its orders with affiliated mills and the remainder with unaffiliated mills. No documentary evidence was submitted to substantiate this estimate, nor was any specific evidence provided by petitioner as to purchases from affiliated versus unaffiliated mills during the years in question. By contrast, the auditor testified he was advised, during the audit, that 85 percent of petitioner's purchases were from affiliated mills.

Petitioner generally purchased steel on a C.I.F. (cost, insurance and freight) basis. In essence, petitioner assumed title and ownership risks when the steel was loaded for shipment. It could, and sometimes did, simultaneously invoice its own customers on the same C.I.F. basis.

Petitioner maintained independent credit with several domestic banks to finance its accounts receivable; it absorbed all losses from unpaid accounts, damaged merchandise, and merchandise which failed to meet the customer's specifications; and it operated an independent credit department which approved or disapproved credit to customers. Inventory maintained by petitioner usually resulted from either cancellation of an order or the withholding of credit to a customer.

(presumably made as an I.R.C. { 482 intercompany adjustment to reallocate intercompany pricing to an "arm's length" basis).

Petitioner maintained its own claims unit. If a customer's claim of defective or damaged merchandise was determined to be a shipping claim, petitioner instituted insurance recovery procedures. If the claim was determined to be a "mill claim", petitioner instituted procedures against the mill. Where mill claims were rejected, petitioner sustained the loss.

OPINION

In the decision below, the Administrative Law Judge found that petitioner was a selling agent of its parent corporation. Accordingly, it was determined that the Division properly recalculated petitioner's business receipts factor by entirely eliminating sales of tangible personal property by petitioner from the computation. As a result, the notices of deficiency were sustained.

On exception petitioner argues that it is a buyer and seller of goods rather than an agent for the manufacturer in its dealings with customers. Specifically, petitioner supports its position arguing that: it receives legal title to the goods, it has no commission agreement with the mills from which it purchases, it acquires equity in the property it purchases, it is obligated to make payment on the goods it purchases, it bears the risk of nonpayment by the customer alone, it bears the risk of loss and has an insurable interest in the goods it buys, it receives the profits from the sale of the goods and it is free to sell the goods at whatever price the market will bear. Petitioner contends that these and other factors support the characterization of it as a buyer-seller rather than an agent. Thus, petitioner concludes that its sales of tangible personal property should be recognized when calculating its business receipts factor, so the notices of deficiency should be appropriately modified.

In response the Division contends that the Administrative Law Judge was correct in finding that petitioner was a sales agent for related mills receiving commission compensation. In support of its position the Division argues that: petitioner's gross profit margin on sales was only one percent, its books and records designated receipts as "commissions", "commissions" exceeded gross profits for two audit years, little or no inventory was maintained, customer orders were subject to the mill's acceptance, orders were for customer accounts and purchased for customer specifications,

customers were billed simultaneously to the mill's billing petitioner, 85% of purchases were from related mills and 100% of petitioner's stock was owned by related companies owning manufacturing mills. The Division asserts that these, among other factors, support the determination that petitioner is a sales agent for related mills receiving commission compensation.

We reverse the determination of the Administrative Law Judge.

Tax Law section 210.3 provides for the allocation of a portion of a taxpayer's entire net income to New York on the basis of a formula consisting of three factors (expressed in percentages): the taxpayer's real and tangible personal property, business receipts, and payroll. The percentages of these three factors result from fractions, the numerator of which is the property, receipts or payroll within New York and the denominator of which is all property, receipts or payroll of the taxpayer. The receipts factor is weighted twice and the four resulting percentages are totaled and divided by four to arrive at the taxpayer's business allocation percentage (20 NYCRR 4-2.2).

In the present case it is the calculation of the receipts factor that is at issue. Tax Law section 210.3(a)(2)(A) and Tax Law section 210.3(a)(2)(B) provide in pertinent part that:

> "The portion of the entire net income of a taxpayer to be allocated within the state shall be determined as follows:
>
> (a) multiply its business income by a business allocation percentage to be determined by
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> * * *
>
> (2) ascertaining the percentage which the receipts of the taxpayer, . . . arising during such period from
>
> (A) sales of its tangible personal property where shipments are made to points within this state,
>
> (B) services performed within the state . . . ."

If subsection (A) applies to the receipts at issue, then the tax due will be substantially less due to the fact that the majority of petitioner's sales are made to points out of state. If subsection (B) applies, then the notices of deficiency would be correct.

In order to make a determination as to whether petitioner's receipts were from sales of tangible personal property or services performed, the Administrative Law Judge based his determination on whether or not an agency relationship existed between petitioner and its related manufacturer. We agree that the existence of an agency relationship is a factor to consider in making our decision. The ultimate decision, however, has its foundation in the characterization of petitioner's receipts pursuant to Tax Law sections 210.3(a)(2)(A) and 210.3(a)(2)(B) as either receipts from the sale of tangible personal property or for the performance of services. We find that the record before us indicates that the receipts at issue were from the sale of tangible personal property.

While Tax Law section 210.3 does not offer a definition of services, 20 NYCRR 4-4.3(b) provides that:

> "Commissions received by a taxpayer are allocated to New York State if the services for which the commissions were paid were performed in New York State. If the services for which the commissions were paid were performed for the taxpayer by salesmen attached to or working out of a New York State office of the taxpayer, the services will be deemed to have been performed in New York State."

Further, 20 NYCRR 4-4.3(b) includes an example for purposes of illustration as follows:

> "A taxpayer is a New York State sales agent of a Pennsylvania manufacturer. A salesman working out of the New York State office of the taxpayer received an order in New Jersey. The order was forwarded to the Pennsylvania manufacturer which accepted it, filled it and shipped it direct to the customer. The taxpayer's commission is allocated to New York State."

Thus, factors indicative of an agency relationship support the characterization as receipts from the performance of services within the State. However, facts that indicate that petitioner took title to property support the characterization as receipts from the sale of tangible personal property.

Since no clear indicia are set forth in either Tax Law section 210.3 or the regulations thereunder, we must look elsewhere for assistance in making our determination. The distinction between an agent and an independent buyer-seller has been generally made as follows:

> "One who receives goods from another for resale to a third person is not thereby the other's agent in the transaction: whether he is an agent for this

> purpose or is himself a buyer depends upon whether the parties agree that his duty is to act primarily for the benefit of the one delivering the goods to him or is to act primarily for his own benefit" (Restatement [Second] of Agency { 14J [1958]).

Several indicia of sale are given to aid in making a determination consistent with the passage above. We find them to be useful in characterizing petitioner for Tax Law section 210.3 purposes. Although no one of the following factors is determinative, each provides evidence of a buyer-seller relationship, which in turn would work to characterize petitioner as a seller of tangible personal property:

1. That the consignee receives legal title and possession of the goods.

2. That the consignee becomes responsible for an agreed price, either at once or when the goods are sold.

3. That the consignee can fix the price at which he sells without accounting to the transferor for the difference between what he obtains and the price he pays.

4. That the goods are incomplete or unfinished and it is understood that the transferee is to make additions to them or complete the process of manufacture.

5. That the risk of loss by accident is upon the transferee.

6. The the transferee deals, or has the right to deal, with the goods of persons other than the transferor.

7. That the transferee deals in his own name and does not disclose that the goods are those of another.

Of the seven factors listed above, we find that all but one are in petitioner's favor. First, petitioner received all documents of title in its own name and had legal title to all goods purchased from both related and unrelated mills. While it is unclear whether petitioner ever received physical possession apart from damaged or returned goods, it is significant that legal title is held in each case even if just for an instance (see, Epic Metals Corporation and Subsidiaries v. Commr., 48 T.C.M. 357).

Second, it is true that contracts of sale were subject to approval of the order by the mill concerned, however, this was true of both related and unrelated mills. Such a process is necessary in a situation calling for specially tailored orders. As a result, we accept petitioner's claim that the statement on the contracts that, "THIS ORDER IS SUBJECT TO OUR MILL'S FINAL ACCEPTANCE" is not indicative of an agency relationship between petitioner and its related mills. Instead, such a clause is an incident to petitioner's sort of business, working to protect it from entering into contracts with customers to purchase specially manufactured goods that may not be readily available from related or unrelated mills. Once approval of the order is received, petitioner's contract with its customers becomes final and petitioner is responsible for the agreed price.

Third, the record indicates that petitioner alone fixed the prices at which it sold to its customers. Specifically, petitioner did not account to its foreign mills for the difference between what it paid and what it received from purchases of the product.

Fourth, the facts neither disclose that the goods are incomplete and unfinished nor is it understood that the petitioner was to make additions to them or complete the process of manufacture. This is the only one of the seven factors that does not support petitioner as a buyer-seller.

Fifth, risk of loss is borne by petitioner according to the facts. Additionally, the facts indicate that petitioner maintained its own insurance coverage on the goods in transit and maintained a claim department and sustained any loss that was not covered by insurance on the products shipped.

Sixth, petitioner has dealt with the goods of other mills than the related mills. Purchases were made from both related and unrelated mills with similar purchase discounts given in each case.

Seventh, the facts indicate that petitioner dealt in its own name with its customers although petitioner did disclose that the goods were received from other mills. This disclosure was consistent with the nature of the goods and seems to have little bearing on the nature of petitioner's activities. As a buyer-seller of custom manufactured goods, petitioner merely protected itself from

the possibility of not being able to fill an order by letting its customers know that since the goods must be purchased from another all orders are subject to the approval of a related or unrelated mill.

While no one of the factors above is conclusive, they must be taken as a whole in characterizing the receipts at issue. Clearly the majority of the factors support the characterization of petitioner as an independent buyer-seller and outweigh the factors that do not favor this position.

Lastly, we note that the factors relied on by the Division to conclude that petitioner was an agent are not persuasive.

First, the Division argues that several of the characteristics of petitioner's business, i.e., the one percent gross profit margin, the fact that commissions exceeded gross profit in some years and the small amount of inventory, are not characteristic of an independent business. The Division directs us to no authority to support its characterization of an independent business or to assist our evaluation of these factors. Accordingly, we decline the opportunity to decide whether these factors are or are not characteristic of a certain type of business.

Next, we note that several of the factors raised by the Division, i.e., that the customers' orders were made subject to the mill's final approval, that orders were made for customer accounts according to customer specification, and that petitioner maintained little inventory, all seem more closely linked to the type of goods sold by petitioner, custom made, than they do to petitioner's status.

The Division also raises the points that petitioner was owned by companies that also owned mills and that 85% of petitioner's purchases were from affiliated mills. The significance of these factors is diminished by the fact that petitioner's purchases from unrelated mills were made in exactly the same fashion as purchases from related mills.

Lastly, the Division asserts that petitioner's characterization of certain amounts as commissions indicates that petitioner was an agent. While we agree that this factor is against petitioner's position, we conclude that it is not sufficient alone to determine that petitioner did not sell tangible personal property.

In summary, the factors raised by the Division do not clearly indicate that petitioner did not make sales of tangible personal property. However, the factors raised by petitioner clearly indicate that it made sales of tangible personal property. While we acknowledge that this case requires a weighing of factors, we conclude, in contrast to the Administrative Law Judge, that petitioner has met its burden and proved that the balance is in favor of petitioner as an independent buyer-seller, making sales of tangible personal property pursuant to Tax Law section 210.3(a)(2)(A).

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Tradearbed, Inc. is granted;

2. The determination of the Administrative Law Judge is reversed; and

3. The petition of Tradearbed, Inc. is granted and the five notices of deficiency issued on August 19, 1985 are cancelled.

Dated: Albany, New York
January 12, 1989

/s/ John P. Dugan
John P. Dugan
President

/s/ Francis R. Koenig
Francis R. Koenig
Commissioner