

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition

of

LASSIE TOGS, INC.

DECISION

for Redetermination **of** a Deficiency or for  
Refund of Corporation Franchise Tax under  
Article 9-A of the Tax Law for the Fiscal  
Years Ended January 31, 1979, January 31,  
1980, and January 31, 1981.

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Petitioner, Lassie Togs, Inc., 112 West 34th Street, New York, New York 10001 filed a petition for redetermination **of** a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the fiscal years ended January 31, 1979, January 31, 1980 and January 31, 1981 (File No. 47485).

A formal hearing was held before Jean Corigliano, Hearing Officer, at the office **of the State** Tax Commission, Two World Trade Center, **New York, New York** on March 20, 1986 at 9:30 A.M., with all briefs to be submitted by July 7, 1986. Petitioner appeared by Harry Wasserman, C.P.A. The Audit Division appeared by John P. Dugan, Esq. (Michael J. Glannon, Esq. of counsel).

#### ISSUE

Whether petitioner properly included the wages of certain individuals in computing its business allocation percentage.

#### FINDINGS OF FACT

1. Petitioner, Lassie **Togs**, Inc. ("Lassie"), filed a State of New York Corporation Franchise Tax Report for each of the fiscal years ended January 31, 1979 through January 31, 1981. On each report, petitioner claimed **a** business allocation which was computed, in pertinent part, by including in its calculations

the wages of five individuals working at the Virginia facilities of a Lassie affiliate.

2. On May 24, 1983, the Audit Division issued three notices of deficiency to Lassie asserting taxes due pursuant to Article 9-A of the Tax Law in the amounts of \$1,487.00 plus interest for the year ended January 31, 1979; \$3,222.00 plus interest for the year ended January 31, 1980; and \$4,637.00 plus interest for the year ended January 31, 1981.

3. On audit, the auditor determined that Lassie had failed to report administrative fees it received for services performed in New York. In addition, the auditor disallowed the wages of the Virginia employees which Lassie had included in calculating its payroll factor. Following a prehearing conference, the Audit Division conceded that the fees should be excluded from receipts because they represented a reimbursement of expenses incurred by Lassie in performing administrative services for affiliated companies; however it rejected the contention that the five Virginia individuals were Lassie employees. The auditor adjusted the payroll factor by subtracting salaries paid to those individuals and allocating 100 percent of Lassie's payroll to New York State. As a result of the conference, the auditor reduced the asserted tax due as follows: \$1,327.00 plus interest for fiscal year ended January 31, 1979; \$2,917.00 plus interest for the fiscal year ended January 31, 1980; and \$3,108.00 plus interest for the fiscal year ended January 31, 1981.

4. Lassie is a subsidiary of Roanna Togs, Inc. ("Roanna"). It markets infants' and small children's clothing and has showrooms, offices and other facilities in New York City for that purpose. Until 1962, Lassie also operated a factory on Long Island where the clothing was produced. Because of an increase in labor related problems, Lassie began looking for an alternative

manufacturing site and eventually opened a new factory in Louisa, Virginia and organized Louisa Manufacturing Corporation ("Louisa") to operate it. At that time, Louisa was a subsidiary of Lassie, but after Roanna's organization both corporations became subsidiaries of Roanna. The officers of all the related corporations are the same individuals.

5. At the time factory operations were moved to Virginia, Lassie's top management wanted to maintain a layer of management between itself and Louisa, as Lassie's comptroller put it, "to have eyes and ears at the factory" loyal to Lassie. Two factory supervisors from New York, the plant manager and cutting room supervisor, chose to move with the manufacturing operation to perform this function. These individuals each had over fifteen years of experience with Lassie and participated in its profit sharing, pension, health benefits and group life insurance plans. Transfer from the Lassie **to** the Louisa payroll would have cost them major losses in benefits. Therefore, in order to smooth the transition and to maintain **a** presence in Virginia, Lassie kept these individuals on its own payroll.

6. During the three years at issue, Lassie maintained five supervisory employees in Virginia: the two individuals described above, the shipping supervisor, the sewing floor supervisor and the quality control supervisor. Lassie withheld **all** federal and state taxes, paid social security and Virginia unemployment insurances and provided fringe benefits, including health and life insurance policies and pension plans, for these five employees. The individuals in question reported directly to Lassie's management by whom they were hired and to whom they were responsible.

7. Louisa reimbursed Lassie for the salaries and payroll taxes expended by Lassie on behalf of these five individuals. This reimbursement was accomplished

in the form of an accounting report entry made on the annual financial statement of Roanna. The comptroller of Roanna and its subsidiaries explained that the entry was intended to provide Roanna's management with information and analysis regarding Louisa and did not represent an actual transfer of assets. Roanna filed a consolidated federal tax return for the years in issue reporting salaries and wages as a consolidated expense and not an expense of a particular corporation.

#### CONCLUSIONS OF LAW

A. That section 210.3 of the Tax Law provides, in part, that a taxpayer's entire net income may be allocated within New York State by multiplying its business income by a business allocation percentage. The business allocation percentage is obtained by a three factor formula consisting of a property factor, a receipts factor and a payroll factor. The payroll factor is computed by:

"ascertaining the percentage of the total wages, salaries and other personal service compensation, similarly computed, during such period of employees within the state, except general executive officers, to the total wages, salaries and other personal service compensation, similarly computed, during such period of all the taxpayer's employees within and without the state, except general executive officers" (Tax Law § 210.3[a][3]).

B. That 20 NYCRR 4-5.2(b) provides that:

"[g]enerally, the relationship of employer and employee exists when the taxpayer has the right to control and direct the individual not only as to the result to be accomplished by him but also as to the means by which such result is to be accomplished. If the relationship of employer and employee exists, the designation or description of the relationship, and the measure, method or designation of the compensation are immaterial."

C. That because the individuals located in Virginia were hired by Lassie, supervised by Lassie and ultimately responsible to Lassie, the individuals were


Law. Since the reimbursement from Louisa to Lassie was merely a financial accounting technique, it cannot be said that Louisa bore the ultimate expense of the five employees. This is consistent with this Commission's decision in Mix 'N' Match of Miami, Inc. (State Tax Comm., January 18, 1985), involving related companies. In that decision, the petitioner (also a Lassie affiliate) sought to exclude from its business allocation percentage reimbursements for salesmen's services paid by Mix 'N' Match to Lassie. There, as here, it **was** determined that Lassie maintained actual control and direction over the employees and that the reimbursement of salaries by Mix 'N' Match to Lassie **was** merely a bookkeeping adjustment not affecting the ultimate determination.

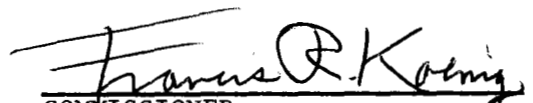
D. That the petition of Lassie Togs, Inc. is granted and the notices of deficiency issued on May 24, 1986 are cancelled.


DATED: Albany, New York

STATE TAX COMMISSION

**SEP 26 1986**

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER