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Corp Tax Determinations

A-Z

BUREAU OF LAW

MEMORANDUM Eastman Kodak Co.

TO: The State Tax Commission

FROM: E. H. Best, Counsel

SUBJECT: EASTMAN KODAK COMPANY

In the matter of the applications for revision or refund of franchise taxes under Article 9-A of the Tax Law for the years 1957, 1958, 1959, 1960, 1961, 1962 and 1963

This case involves the construction of the language used in section 210(3)(a)(2) of the Tax Law with respect to the words "an order shall be deemed received or accepted within the State, if it has been received or accepted by an employee, agent or agency or independent contractor, chiefly situated at, connected with, by contract or otherwise, or sent out from a permanent or continuous place of business of the taxpayer within the State". More specifically, a construction of the words "connected with" and the word "chiefly" is necessary. The proposed determination holds that orders were received or accepted by an independent contractor chiefly connected with, by contract or otherwise, a permanent or continuous place of business of the taxpayer within the State.

The facts are briefly as follows:

During the years 1957 through 1963, Eastman Kodak Company, which has its principal office, a permanent and continuous place of business, in Rochester, New York and has three branch offices, two of which are outside the State, entered into a contract with two foreign corporations having offices outside the State, to sell Kodak's supply of unexposed professional motion picture film. The two foreign corporations are independent contractors having no office in this State. They obtain technical advice with regard to the technical capability of the film from the taxpayer's branch offices. The branch offices do not sell any of the film.

The facts disclose that the principal office in Rochester, pursuant to the contract naming the independent contractors as the exclusive sales agency for the period involved, has the following rights:

A. Establish and maintain list of film to be sold by the agent.

B. Establish and revise prices at which agent shall sell.

C. Establish equitable adjustment for cash discounts.

D. Receive agent's weekly reports of and payments for sales.

E. Weekly inventory replenishment and inspection of inventories at agent's warehouses.

F. Emergency shipments direct to customers on order of the agent.

G. Provide inventory insurance.

H. Accept and maintain agent's deposit of sum equivalent to eight days sales (minimum $1,500,000).

I. All notices, statements, communications to and from Rochester office.

J. Right to cancel agreement.

The taxpayer omitted from the numerator of the receipts factor certain sales made on the ground that these were made by an independent contractor not chiefly connected with a permanent or continuous place of business of the taxpayer within the State. Although it is obvious that Kodak has a permanent and continuous place of business in the State and sales were made out of the State by the independent contractor, the taxpayer contends that the independent contractors are not connected with its Rochester office, or if connected, are more closely connected with permanent places of business outside of the State and thus are not chiefly connected with a permanent place of business at Rochester, New York.

The words in dispute were added by Chapter 603 of the Laws of 1948. Prior to such time, the herein situation would have resulted in the exclusion from the receipts factor of the sales made by the independent contractors since they were received or accepted by the independent contractor outside of the State.

The bill as originally proposed would have included sales allocable to New York State where the orders were received by an agent outside of the State if "(1) the agent was chiefly situated at, connected with or sent out from a permanent or continuous

place of business of the taxpayer within the State and (2) where the taxpayer has a permanent or continuous place of business within the State by an agent not chiefly situated at, connected with or sent out from a permanent or continuous place of business of the taxpayer without the State. The final bill as passed eliminated the second situation.

The taxpayer contends, in his memorandum, that the elimination of the last situation shows that the intent of the statute was that sales made by out-of-state locations of independent sales agents were not to be reflected as New York sales for New York franchise tax apportionment purposes and refers for its interpretation to a letter from Alger B. Chapman, former Commissioner of Taxation and Finance, written on March 27, 1948. It is apparent that the letter has been misinterpreted. The tenor of the letter shows that whereas such sales would have been deemed received or accepted without the State prior to the amendment, the intent of the department was to include such sales as accepted within this State and accordingly to urge the passage of the amendment effectuating such treatment.

It is to be noted that Missouri, Pennsylvania, Massachusetts and Utah have provisions in their tax laws which are converse to the provisions in the New York State statute. The statutes of these states provide, in effect, that sales effected by agents or agencies chiefly situated at, connected with or sent out from, premises for the transaction of business maintained (or owned or rented) by the taxpayer outside the state are to be excluded from the numerator of the receipts or sales factor. Cases arising in foreign jurisdictions are cited by the taxpayer to support his contention that the independent contractors are not chiefly connected with the Rochester office of the taxpayer.

The cases hold that (a) where the taxpayer has a sales office in the taxing jurisdiction and sales personnel were supervised from that sales office or sales were solicited by agents dispatched from such office that the personnel or agents were chiefly connected with an office of the taxpayer located in the taxing jurisdiction, Commonwealth v. Bayuk Cigars, 345 Pa. 348, 28 A. 2d 134, 138 (1942); State Tax Commission v. John H. Breck, Inc., 366 Mass. 144, N.E. 2d 87, 96, 101 (1957); Maytag Co. v. Commissioner of Taxation, 218 Minn. 460, 463, 17 N.W. 2d 37, 40 (1944) and Twentieth Century-Fox Film Corporation v. Phillips, 76 Ga. App. 825, 47 S.E. 2d 183 (1948) and (b) where the taxpayer maintained an office in the home state but maintained a branch office

in foreign states where orders were solicited by salesmen working out of that branch office, Commonwealth v. Continental Rubber Works, 347 Pa. 514, 32 A. 2d 878 (1943), or sales were made by an agent located at the foreign plant of the taxpayer, Commonwealth v. Charles S. Walton & Co., 53 Dauph. Co. Rep. (Pa.) 279, 288, 292 (1942) the agent is chiefly connected with the out-of-state branch or place of business.

The decisions of these jurisdictions are in conformity with New York treatment. If the taxpayer has both offices within and without the state, the chief connection would be with that office of the taxpayer from which its sales personnel are sent or supervised or out of which office the agent is located. The chief connection would, therefore, be with a sales office of the taxpayer. These conclusions are also followed in the cases of Kennecott Copper Corporation v. State Tax Commission, 5 Utah 2d 306, 316, 301 p. 2d 562, 569 (1956) and F. M. Stamper Co. of Minnesota v. Commissioner of Taxation, CCH Minn. Tax Service (1963), Par. 200-280 (June 18, 1963).

The statement of facts in the last two cases, as set forth by the taxpayer in his memorandum, could lead one to the conclusion that where the taxpayer has an office in the taxing jurisdiction but an independent sales agent has a sales office outside of the jurisdiction, sales could not be connected with the taxing jurisdiction. A reading of the cases show, however, that the taxpayer was either the parent or wholly owned subsidiary of the sales corporation, that the taxpayer and the sales corporation were located in the same branch office outside of the State and that accordingly the only conclusion that could be reached was that the agent was chiefly connected with such office outside the State. It is to be noted that in the instant matter under review, the branch offices of the taxpayer located without New York could not sell the products of the taxpayer and could only give advice on the technical aspects of the product.

The case of Commonwealth of Pennsylvania v. Minds Coal Mining Corporation, Court of Common Pleas, Dauphin County, Decided December 24, 1946 Pennsylvania Tax Reporter, Par. 200-020, aff'd 369, Pa. 7, 66, A. 2d 14 (1948) which is cited by the taxpayer in support of his contention, tends to support the position taken in this determination. In that case where the taxpayer maintained its executive offices in Pennsylvania but sold coal in New York State through an independent sales agent which had its own offices and its own salesmen, the court held that the sales were allocable to the taxing state, Pennsylvania in that the sales agent was not connected with any branch office located in New York State. Kodak argues that the Pennsylvania court decided "that sales were chiefly connected with the New York premises of the independent sales agent".

The connection required to be ascertained by the New York statute is not whether there was a connection with the premises of the independent agent (there always is) but whether there was a connection with that of the taxpayer. In the Minds Coal Mining Corporation, supra, case, the court answered by saying there was no connection with the taxpayer in New York State since the taxpayer did not maintain an office there. The sales were therefore allocable to Pennsylvania where the home office was located.

The Minds Coal Mining Corporation, supra, case distinguishes between the New York State statute and those of the foreign jurisdictions. In the foreign jurisdictions where there is no chief connection with a place of business of the taxpayer outside of the state, the sales are allocable to the home state. No showing need be made that there is a chief connection with a place of business in the home state in order to include such sales as allocated to the home state. Under the New York statute, such chief connection is necessary. By virtue of such distinction, the laws of the aforesaid foreign jurisdictions and the proposed amendment as originally drafted would be more drastic to a taxpayer seeking to exclude sales made by an agent in a foreign state. However, as heretofore stated, the purpose of the amendment to the statute was to include as allocable to New York sales made under situations like the present, which were previously not allocable to this State. The chief connection with the Rochester office is shown by the supervision and control maintained pursuant to contract by the taxpayer's Rochester office over the sales activities of the independent contractors.

I am, therefore, of the opinion that the independent contractors were chiefly connected with the taxpayer's permanent and continuous place of business in New York State and that consequently, the orders were received and accepted in this State. If you agree, kindly sign the proposed determination and return to the Law Bureau for further processing.

/S/ E. H. BEST
Counsel

MS:kon
Enc.

March 26, 1968

4-1-68

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Applications

of

EASTMAN KODAK COMPANY

for revision or refund of franchise taxes under Article 9-A of the Tax Law for the years 1957, 1958, 1959, 1960, 1961, 1962 and 1963

Eastman Kodak Company, the taxpayer herein, having filed applications for revision or refund of franchise taxes under Article 9-A of the Tax Law, and the facts having been agreed to by Stipulation of Facts, dated December 23, 1966, executed by Edward H. Best, Counsel and Deputy Tax Commissioner of the State Tax Commission, and by Harmar Brereton, Vice President and General Counsel, for the taxpayer, and the parties having waived the right to present any further testimony at a formal hearing under section 214 of the Tax Law,

Upon all the stipulated facts herein and upon the entire record, it is hereby found:

(1) The taxpayer, Eastman Kodak Company, a New Jersey corporation doing business in the State of New York is engaged in the manufacture and sale of unexposed professional motion picture films among other items. The taxpayer has a permanent and continuous place of business in Rochester, New York where its principal and home office is located. In addition thereto, the taxpayer maintains branch offices in New York City, in Hollywood, California and Chicago, Illinois, which offices are professional motion picture film department offices engaged in technical research and product development and improvement.

(2) During the years in issue, the taxpayer sold unexposed motion picture film of its manufacture through W. J. German, Inc., a Delaware corporation, having its principal place of business in Fort Lee, New Jersey and W. J. German, Inc., a California corporation, having its principal place of business in Hollywood, California, pursuant to and under contracts dated January 1, 1957 and January 1, 1961 entered into between the taxpayer and the aforesaid independent contractors at the taxpayer's principal office in Rochester, New York. The 1957 contract, in effect during the years 1957 through 1960, and the 1961 contract, in effect during the years 1961 through 1963, are substantially similar and are hereinafter designated as "the contract". During the years in issue, the aforesaid independent contractors, hereinafter called "Agent", owned substantial offices and warehouses in Fort Lee, New Jersey; Chicago, Illinois and Hollywood, California.

(3) The taxpayer filed New York franchise tax returns for the years in issue in which returns the taxpayer was required to compute the percentage of total receipts which were attributable to this State. The percentage is computed by dividing a numerator consisting of receipts attributable to this State, by a denominator consisting of the total receipts within or without the State, pursuant to the provisions of section 210(3)(a)(2) of the Tax Law. The pertinent provisions of such section in effect during the years 1957 through 1960 are:

> "3. The portion of the entire net income of a taxpayer to be allocated within the state shall be determined as follows:
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> (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, computed on the cash or accrual basis according to the method of accounting used in the computation of its entire net income, arising during such period from

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(B) sales of any such property not located at the time of the receipt of or appropriation to the orders at any permanent or continuous place of business maintained by the taxpayer without the state, where the orders were received or accepted within the state and for purposes of this clause an order shall be deemed received or accepted within the state if it has been received or accepted by an employee, agent, agency or independent contractor chiefly situated at, connected with, by contract or otherwise, or sent out from a permanent or continuous place of business of the taxpayer within the state.

* * * * * *

(E) all other business receipts earned within the state, bear to the total amount of the taxpayer's receipts, similarly computed, arising during such period from all sales of its tangible personal property, services, rentals, royalties and all other business transactions, whether within or without the state;"

The pertinent provisions of section 210(3)(a)(2) of the Tax Law, in effect for the years 1961 through 1963, are:

"3. 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, computed on the cash or accrual basis according to the method of accounting used in the computation of its entire net income, arising during such period from

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(B) sales of its tangible personal property not located at the time of the receipt of or appropriation to the orders at any permanent or continuous place of business maintained by the taxpayer without the state where the orders were received or accepted within the state and where shipments are made to points within the state,

> (C) . . . . sales of its tangible personal property (except sales described in clause B) located without the state at the time of the receipt of or appropriation to the orders where shipment is made to points within the state, but only to the extent of fifty per centum of the receipts from the sale referred to in this clause,
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> (D) sales of its tangible personal property not located at the time of the receipt of or appropriation to the orders at any permanent or continuous place of business maintained by the taxpayer without the state, where the orders were received or accepted within the state and where shipment is made between points outside the state, but only to the extent of fifty per centum of the receipts from the sales referred to in this clause. For purposes of this clause and clause B an order shall be deemed received or accepted within the state if it has been received or accepted by an employee, agent, agency or independent contractor chiefly situated at, connected with, by contract or otherwise, or sent out from a permanent or continuous place of business of the taxpayer within the state,
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> (G) all other business receipts earned within the state, bear to the total amount of the taxpayer's receipts, similarly computed, arising during such period from all sales of its tangible personal property, services, rentals, royalties and all other business transactions, whether within or without the state;"

(4) In computing the receipts percentage, the taxpayer omitted from the numerator all of its sales which were made through "Agent" during the years 1957 through 1960. For the years 1961 through 1963, the taxpayer included in the numerator only 50% of the sales made through "Agent" of film delivered to customers within New York State, and omitted from the numerator, sales made through "Agent" of film delivered to customers outside of New York State; that such computations were made by the taxpayer on its contentions that no orders were deemed received or accepted within the State and the orders were received by an "Agent" or independent contractor not chiefly situated at,

connected with, by contract or otherwise, from a permanent place or continuous place of business of the taxpayer within the State.

(5) The State Tax Commission in construing the provisions of section 210(3)(a)(2)(B) of the Tax Law, in effect during the years 1957 through 1960, issued assessments for the years 1957 through 1960, adding to the numerator the amount of sales omitted by the taxpayer for such years. For the years 1961 through 1963, the State Tax Commission in construing the provisions of section 210(3)(a)(2)(B) and (D) of the Tax Law, in effect during such years, issued assessments adding to the numerator 100% of the sales of film delivered to customers in the State, which sales were reported by the taxpayer to the extent of 50% only, and adding to the numerator 50% of the sales of film delivered to customers outside the State, all of which sales were omitted by the taxpayer; the assessments with respect to all of the years in issue were based on the ground that "Agent" was an independent contractor chiefly connected by contract or otherwise with a permanent or continuous place of business of the taxpayer within the State within the intent and meaning of such provisions contained in section 210(3)(a)(2) of the Tax Law.

(6) Pursuant to the contract, inventories of film to be sold by "Agent" were kept in warehouses maintained by "Agent". Film sold by "Agent" was sold from these inventories and was not located at any permanent or continuous place of business maintained by the taxpayer outside of New York State. Title in such film was to reside in the taxpayer at all times until it passed to the customers upon delivery by "Agent". The inventories were originally furnished and replenished from time to time by taxpayer's Rochester office. "Agent" maintained the inventory control including its estimates of future inventory requirements. The taxpayer had the right to have representatives present when "Agent" took physical inventory, and to have "Agent's"

inventory records available for inspection by the taxpayer's representatives. Once a year, personnel of the independent certified public accounting firm employed by the taxpayer's Rochester office would be present when "Agent" took physical inventory at "Agent's" locations at Hollywood, Chicago and Fort Lee, New Jersey, and reports of such accountants were then furnished to taxpayer's Rochester office. In the event of an inventory shortage, "Agent" was required to pay the taxpayer's Rochester office for the shortage, a sum equivalent to the value of such shortage, calculated at the prices set forth in the appendix to the contract, less the applicable commissions, unless the shortage was due to a loss covered by fire and extended coverage insurance maintained by taxpayer. Questions arising in connection with inventory shortages were decided by taxpayer's executives employed at the taxpayer's Rochester office. The inventories of film in "Agent's" warehouses were insured under policies purchased by the taxpayer's Rochester office.

(7) The contract further provided that the film was to be sold at prices set forth in the appendix to the contract and that the taxpayer had the right to amend prices. Decisions to amend prices were made by the taxpayer's executives employed at the Rochester office and the "Agent" was notified of the changes by such Rochester office. During the years 1957 through 1961 prices were amended by taxpayer's Rochester office three times.

(8) Pursuant to the contract, "Agent" established the terms and cash discounts with respect to the sale of Kodak film under the contract and earned a commission with respect to all film sold through "Agent". The taxpayer's Rochester office,

in its discretion, under the contract, had the right to allow "Agent" equitable adjustment for any cash discount which "Agent" allowed purchasers, not exceeding 3%. The taxpayer's Rochester office authorized an adjustment at the commencement of the first contract with "Agent" in 1952, and during the years 1957 through 1963, there was no change in the adjustment. Had there been a change in the adjustments such change would have been handled and authorized through taxpayer's Rochester office.

(9) "Agent" directed sales, solicitation and promotion of the taxpayer's film products and received and accepted the orders from the customers. All billing was done by "Agent's" personnel who maintained their accounts for each customer and collected the payments from the customers. "Agent" filled the orders and shipped the orders to the customers or delivered the merchandise to the customers at "Agent's" locations. On occasion emergency shipments were made directly to customers from taxpayer's Rochester plant.

(10) In all of the activities set forth in finding of fact (8), "Agent's" employees were supervised, directed and controlled by "Agent" and not by the taxpayer. "Agent's" management hired and discharged "Agent's" personnel and said personnel were paid by "Agent" and not by the taxpayer. All of the "Agent's" personnel worked out of "Agent's" locations and no personnel of the taxpayer's worked out of "Agent's" locations. Each of "Agent's" buildings were owned by "Agent" and was clearly identified by "Agent", bearing "Agent's" name. All telephone listings and other classification listings for "Agent's" premises were in "Agent's" name only. All of "Agent's" operating expenses were paid by "Agent" and "Agent" did not account to the taxpayer for its expenses.

(11) "Agent" furnished the taxpayer's Rochester office with "Agent's" management's annual forecasts of the products required for use in production planning. "Agent" furnished the

taxpayer's Rochester office with weekly summary reports covering total sales made through "Agent" (no separate reports giving information as to sales made to individual customers were furnished). Although there were no audits of these reports by the taxpayer, any decision to audit would have been made by the taxpayer's executives whose headquarters were in Rochester.

(12) The remittances from customers from "Agent's" Hollywood office were deposited in taxpayer's account in Los Angeles. The remittances from "Agent's" Fort Lee and Chicago offices were deposited in the taxpayer's account in New York City. Reports of all the remittances were furnished to the taxpayer's Rochester office.

(13) In order to secure the remittances, the contract provided for a security deposit to be made by "Agent". The security deposit was made by "Agent" in taxpayer's account at Chemical Bank New York Trust Company in New York City. Reports on the account were sent by the bank to taxpayer's office at Rochester. Any questions arising with respect to security deposits were decided by the taxpayer's executives whose headquarters were in Rochester.

(14) The contract between the taxpayer and "Agent" which was drafted and negotiated by the taxpayer's general counsel in Rochester and "Agent's" counsel and signed and accepted by the taxpayer in Rochester, provided that notices were to be conclusively deemed to have been given as sent to the taxpayer in Rochester or to "Agent" in Fort Lee, New Jersey. However, during the years in issue no formal notices were sent by either of the parties to the other. Any question concerning the rights and obligations of the parties under the contract was under the jurisdiction of the taxpayer's Rochester office. Under the contract, the taxpayer had the right to terminate the contract under certain conditions, and the contract was terminated at the

end of 1963, pursuant to exercise by the taxpayer of its right to terminate. The decision to terminate was made by the taxpayer's executives whose headquarters were in Rochester.

(15) In contacts with customers, "Agent's" personnel determined whether customers were encountering problems with the taxpayer's film and "Agent" communicated such information to the taxpayer's branch offices in Hollywood, Chicago and New York City. The taxpayer's branch offices did not sell any film which was sold solely by the "Agent" under the contract but received requests for assistance on technical matters with respect to such film either from the customer or from the "Agent". In general, the New York City, Chicago and Hollywood branch offices of the taxpayer served the same general area as did "Agent's" Fort Lee, Chicago and Hollywood offices respectively. These professional motion picture film department offices were under the general supervision of the taxpayer's Rochester office and the managers of the East coast division, the Midwest division and the West coast division of the taxpayer's professional motion picture film departments had contacts with "Agent's" personnel in the respective areas serviced by the divisions for the purpose of enabling (1) "Agent's" personnel to inform the taxpayer's personnel of "Agent's" then prevailing sales policies, and pass on to the taxpayer's personnel any technical problems or complaints raised by customers, so that taxpayer's personnel could work on solution of such technical problems and resolution of such complaints; and (2) the taxpayer's personnel to report to "Agent's" personnel on technical developments in the field, and pass on to "Agent's" personnel, for disposition as "Agent's" personnel saw fit, any sales problems coming to the attention of the taxpayer's personnel.

(16) Face to face contacts with the taxpayer's executives who work out of the taxpayer's Rochester office occurred once a year when "Agent" and taxpayer's personnel met in Rochester with other Kodak management personnel to discuss matters of common interest and future plans, and when the taxpayer's executives including the manager of the professional motion picture department, who worked at and out of the Rochester office, visited and spent time at the branch offices. During the course of visits by the taxpayer's executives, the taxpayer's executives called on customers to service complaints and solicit suggestions about the product but did not call for the purpose of selling film.

Based upon the foregoing, the State Tax Commission hereby,

DETERMINES:

(A) "Agent" was, during the years in issue, independent contractors and received or accepted orders for sale of the taxpayer's tangible personal property; that such tangible personal property was not located at any permanent or continuous place of business maintained by the taxpayer without the state; that taxpayer's Rochester office was, during such years, a permanent and continuous place of business within the State.

(B) That the independent contractors were chiefly connected with, by contract or otherwise, taxpayer's Rochester office located in the State.

(C) That accordingly, the orders were received or accepted within this State and were properly allocable within the State under the provisions of section 210(3)(a)(2)(B) of

the Tax Law for the years 1957 through 1960, and under the provisions of section 210(3)(a)(2)(B) and (D) of the Tax Law for the years 1961, 1962 and 1963.

(D) That the business allocation percentage as determined properly reflected the activity, business, income or capital of the taxpayer within the State during the years in issue.

(E) That the taxes for the years 1957 through 1963 are affirmed as assessed, and do not include any taxes or other charges which are not legally due.

DATED: Albany, New York 10th day of April , 1968.

STATE TAX COMMISSION

/s/ JOSEPH H. MURPHY
President

/s/ A. BRUCE MANLEY
Commissioner

/s/ SAMUEL E. LEPLER
Commissioner