

February 9, 2005

05-001  
NAME  
ADDRESS  
PHONE

Dear TP REPRESENTATIVE:

We represent a client (“Company A”) who desires a written legal opinion with respect to the application of sales and use tax in your state with regards to the following transactions:

### **BACKGROUND**

Company A is a retailer and wholesaler of tangible personal property. Company B, a retailer and wholesaler of tangible personal property, desires to enter into an agreement with Company A such that Company A will provide one of the following services:

#### **Service #1 – Distribution Services**

Company B has merchandise which it wishes to distribute and sell. Company B would like to hire Company A to supply order processing, customer service, credit and collections, data processing, shipping, and warehousing services. We note that Company B’s products are not sold by Company A and Company B may sell its products via other distribution channels. These services are described as follows:

- Order processing – Company A will accept and process orders placed via Company B’s website, mail order, telephone or fax. Payments by check are made out to Company B c/o Company A. Payments by credit card will show Company A’s name and 800 telephone number as reflected by the credit and collections service provided by Company A. Invoices or receipts will reflect Company A’s name and address but will also state on the invoice that the invoice includes merchandise from Company B. It is possible that the invoice will include merchandise from Company A and Company B.
- Customer service – Any merchandise returned by customers will be sent to Company B c/o Company A at Company A’s address.
- Credit and collections – Billing and collections activity will be performed under Company’s A’s returns and collections policies. Company A will determine granting of credit to Company B customers under its own credit policies. Company B may at its own risk override Company A’s credit hold decision on a specific account and grant credit for Company B’s own merchandise in writing. Company A will use all reasonable efforts to collect on Company B’s accounts consistent with efforts made to collect

from its own customers, including but not limited to using collection agencies and attorneys. Company A will provide on-line access to records which document collection efforts made by Company A to collect on delinquent Company B accounts.

- Data processing and Inventory Management – Company A will provide sales, royalty, direct mail, customer mailing list, inventory, A/R and other reports to Company B. Company A will count incoming merchandise and report actual numbers as well as any damaged goods received, promptly so that Company B can adjust figures on vendors' invoices. Company A will not release incoming merchandise from inventory until written authorization is received from Company B. Company A will apply Company B's write-down policy to Company B's write down policy to Company B's inventory at the end of each month and provide a report showing revised inventory values.
- Shipping – Company A will ship all Company B's orders with postage based on purchase amount for direct mail and individual orders charged to customers. For all other customers, the actual postage is billed to them. Company A primarily ships by trackable means unless the customer accepts responsibility if shipped by an alternate method.
- Warehousing – Company A will store, care for and provide warehouse space for all Company B merchandise. Company B will ship its merchandise to Company A's warehouse. Insurance on Company B's inventory while warehoused at Company A's warehouse will be the responsibility of Company B. There is no requirement for Company A to insure any of Company B's inventory, however, Company A has the responsibility to provide reasonable care and accountability for Company B's inventory at Company A's facilities. Company A does not take title to Company B's merchandise.
- Fees and other conditions – Company A's fee for these services provided will be a percentage of net sales of Company B's products fulfilled by Company A. Company A will forward a check for all monies collected for Company B for each month.
- Upon termination of this distribution agreement, Company B will remove its inventory from Company A warehouses. Payment by Company A to Company B will be continued until all outstanding receivables are transferred to Company B for collection. Subsequent payments after transfer of outstanding receivables will be promptly forwarded to Company B. Company A will deliver electronic files containing all Company B data stored by Company A to Company B within thirty (30) days.

Editorial, production, design, marketing, sales, pricing, subsidiary rights, and contractual matters remain strictly the province of Company B. Company A's obligations under this distribution agreement are limited solely to the warehousing, distribution, and other services and activities as

described. Any additional distribution activities undertaken by Company B must first be approved by Company A.

Company B will provide copies of its catalogs, price lists, brochures, and other information as reasonably requested by Company A to enable Company A to perform its obligations under this distribution agreement.

Nothing contained in the distribution agreement shall be construed to place the parties in the relationship of partners or joint ventures, it being agreed and understood that Company A is an independent contractor and is not an agent or employee of Company B. Company A shall have no power to obligate or bind Company B in any manner whatsoever.

### **Service #2 – Exclusive Distribution, General Marketing and Sales Services Agreement**

In addition to the services provided above, Company A will also provide promotion, publicity, advertising and sales representation. Company A will be the sole and exclusive distributor of Company B's merchandise but does not take title to such merchandise.

Such promotion, publicity and advertising services include:

- Inclusion in catalogs which are mailed to customers as well as used in personal sales calls by representatives and agents of Company A.
- Company B's products will be listed on Company A's website.
- Company B's products will be included in special promotions and events with Company A's products.

Company A's fee for these services provided will be a percentage of net sales of Company B's products fulfilled by Company A.

### **QUESTIONS**

1. Based on the facts described above, which party (Company A or B) would your state consider to be the retailer and thus subject to a sales and use tax registration and filing requirement for Service #1 and Service #2?
2. Would your answer to Question #1 be different if:
  - a. Only Company A is registered or has sufficient nexus in your state for sales and use tax registration purposes?
  - b. Only Company B is registered or has sufficient nexus in your state for sales and use tax registration purposes.
  - c. Both Company A and B are registered or have sufficient nexus in your state for sales and use tax registration purposes?
3. Would you answer to Question #1 or #2 be different, if the property was shipped from a warehouse located in your state?

4. Would your answer to Question #1 or #2 be different, if the property was shipped from a warehouse located outside of your state?

Thank you for your consideration in this matter. Should you have any questions, I may be reached at  
PHONE NUMBER

Sincerely,

TAXPAYER

## **RESPONSE LETTER**

DATE

NAME  
ADDRESS  
PHONE

Re: Private Letter Ruling Request-Retail Sales/Distribution Agreement

Dear TAXPAYER:

We have received your request for a private letter ruling concerning tax liability associated with a distribution and marketing arrangement between your client (“Company A”) and another company which is a retailer and wholesaler of tangible personal property (“Company B”). In your letter you have outlined the possible agreements between Company A and Company B and have asked four questions concerning which company would be considered the “retailer” and thus subject to sales and use tax registration and filing requirements.

### **Terms of Agreements**

#### **Distribution Services Agreement**

Company B hires Company A as an independent contractor to accept and process orders of Company B’s merchandise. Company B will ship the merchandize to Company A, who will store, care for, warehouse and provide inventory management. Title to the merchandise will not transfer to Company A, and Company B will be responsible for insuring the merchandise while it is located in Company A’s warehouse. Company A will process orders placed via internet, mail order, telephone or facsimile by invoicing, collecting the purchase price and shipping the merchandize to the customer. Company A may include its own merchandise with the order and on the same invoice as Company B’s merchandise. In addition Company A will provide customer service. Company A’s

fee for the services will be a percentage of net sales of Company B's merchandise. Company B determines the pricing. Company B will provide copies of catalogs, price lists, brochures and other information to Company A as necessary.

#### Exclusive Distribution, General Marketing and Sales Services Agreement

In addition to the services provided pursuant to the Distribution Services Agreement, Company A would provide promotion, publicity, advertising and sales representation. This would mean inclusion in special promotions with Company A's product as well as listed on Company A's website. Company B's merchandise would be included in catalogs and personal sales calls. Company A will be the sole and exclusive distributor of Company B's merchandise but does not take title to the merchandise.

#### Applicable Law

Before addressing your specific issues, we should summarize the relevant law applicable to your general situation. Utah law levies a tax on all nonexempt retail sales within the state. See Utah Code Sec. 59-12-103. You have asked which party would be considered the "retailer." (Pursuant to 59-12-107, the appropriate terminology is "seller" rather than "retailer.") Utah Code Sec. 59-12-107(1)(a) provides that the "seller" shall pay or collect and remit the sales and use tax imposed if the seller has or utilizes certain connections to the state or engages in certain business activities within the state. The requirement is imposed if the seller:

- (i) has or utilizes:
  - (A) an office;
  - (B) a distribution house;
  - (C) a sales house;
  - (D) a warehouse;
  - (E) a service enterprise; or
  - (F) a place of business similar to Subsections (1)(a)(i)(A) through (E);
  
- (ii) maintains a stock of goods;
  
- (iii) regularly solicits orders, regardless of whether or not the orders are accepted in the state, unless the seller's only activity in the state is:
  - (A) advertising; or
  - (B) solicitation by:
    - (I) direct mail;
    - (II) electronic mail;
    - (III) the Internet;
    - (IV) telephone; or
    - (V) a means similar to Subsections (1)(a)(iii)(A) or (B);
  
- (iv) regularly engages in the delivery of property in the state other than by:
  - (A) common carrier; or

(B) United States mail; or

“Seller” is defined at Utah Code Sec. 59-12-102(72) “as a person that makes a sale.” A definition of “sale” is provided at Sec. 59-12-102(66) and refers to transfer of title for consideration. Although sales and use tax is the liability of the purchaser, the “seller” is responsible for collecting and remitting the tax to the state if the “seller” has nexus in Utah.

An agent or independent contractor with Utah nexus acting on behalf of the seller is sufficient to create nexus for the seller. We find that the activities you describe that your client, Company A, engages in on behalf of Company B constitute an agency relationship.

### **Specific Questions**

#### **Question 1. Which company is the retailer (seller)?**

You asked which party, Company A or Company B, would be considered the retailer and thus subject to sales and use tax registration and filing requirement. As title is transferred from Company B to the customer, Company B is the seller. However, Company A, as the agent, is acting on behalf of Company B. This would be the same under either of the distribution agreements described above. If either Company A or Company B has nexus, Company B is liable for the sales tax and Company A acting on behalf of Company B must collect sales tax on Company B’s Utah sales.

With respect to registration requirements under Sec. 59-12-106, and assuming that either or both of the companies have nexus in Utah, since they are acting in concert through the agency relationship, the Commission recommends that both register in Utah. As we discuss further below, both companies are equally liable for the collection and remittance of sales taxes. Company A would be required to register since it solicits orders, and might possibly take payments, on behalf of Company B. Company B is required to register since it is ultimately the seller.

However, despite that both Company A and Company B are equally liable for collection and remittance of the sales tax and should register, only one should report the transactions. Which of the two companies remits the tax on these transactions to the Tax Commission may depend on the contract or agreement between the two companies. The Tax Commission would recommend that the companies delineate in their agency relationship agreement which company will report and remit the sales tax for the transactions.

#### **Question 2. Nexus**

In your second question you ask if the answer to Question 1 would be different if only Company A was registered and had nexus in this state, or if only Company B was registered and had nexus. As noted above it does not matter as far as the liability for sales tax if one or the other company has nexus. If Company A has nexus this is sufficient to create nexus for Company B. For your further information, as noted above the actual remittance to the Tax Commission may depend on the contract or agreement between the parties. Company A may be required under the terms of its agreement with Company B to report and remit the tax to the Utah State Tax Commission on Company B's behalf, keeping in mind that Company B may be held liable if Company A fails to remit. If the agreement requires that Company A only collect the tax and then turn it over to Company B, Company B must report and remit the tax collected.

### Question 3. Warehouse in Utah

Your third question is whether it would make a difference if the property is shipped from a warehouse located in Utah. If the inventory is shipped from a Utah location nexus is clearly established. Tax would have to be collected as indicated in the answer to Questions 1 & 2.

### Question 4. Warehouse outside Utah

Your final question was whether it would make a difference if the property were shipped from a warehouse located outside Utah. For this we refer you back to the first answer. If either company has nexus with Utah through some contact, sales tax would have to be collected on the sales.

In addition it should be noted that any sales or use tax collected from customers must be collected on the entire taxable invoice amount without any reduction for services performed by Company A.

As a final concluding note, we would point out that the tax collection must be included with the customer's payment. If the tax is not remitted, the Tax Commission has the right to take collection actions against either company.

We hope this information satisfies your request. You may contact us if you have further questions.

For the Commission,

Marc B. Johnson  
Commissioner