

CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 242

October 28, 1959

ALLOCATION: EMPLOYEES VS INDEPENDENT CONTRACTORS

Syllabus:

(1) Sales of merchandise shipped to California should be apportioned to the State for purposes of the sales factor in the allocation formula only when the corporations California representatives are employees.

(2) In the present case the company's California representatives were found to be independent contractors.

X Corporation is a foreign corporation and has its head office in New York City. It is represented in California by some five individuals who call on the retail trade to take orders for the Company's products.

The governing principle of allocation is that apportionment is to be made on the basis of the taxpayer's activity. Furthermore, it is settled that the activity of an independent agent of the taxpayer is not attributable to the taxpayer. Irvine v. McColgan, 26 Cal. 2d 160; El Dorado Oil Works v. McColgan, 34 Cal. 2d 731; Appeal of Farmers Underwriters Association, February 18, 1953; Appeal of the Times-Mirror Co., October 27, 1953; Appeal of Caltex Sportswear Co., January 20, 1954; Appeal of Snap-On Tools Corp., December 29, 1958.

The test of an independent agent is the degree of control or right to control that is or may be exercised over the performance of his work, that is, whether there is direction and control over the detail, method, manner, or means of performance or only over the results to be accomplished. U.S. v. Silk, 331 U.S. 704, 91 L. Ed. 1757; Benson v. Social Security Board, 172 Fed. 2d 682, 37 AFTR 914; Irene L. Bell, 13 TC 344; cf. John A. Radovich, 12 TCM 1121,

The sales representatives in the instant situation appear to have complete control over the use of their time and the methods and routine followed in the performance of their work. The company appears to be interested only in the results of their performance, that is, the volume of sales produced. They do not appear to be supervised in any manner by the company except as to the territory allotted to them. They are compensated solely on the basis of the success of their efforts and must bear all of the expenses of carrying on their activities. Thus, their income or profit is largely subject to their own effort and control, and they bear all of the risk. They are not subject to payroll deductions and are considered to be independent contractors by the company. They appear to have complete discretion in calling on accounts and in

seeking new accounts as well as in determining the amount of expense to be incurred by them in promoting business. The company has no office or listing in this State nor does it have a sales supervisor here. On the basis of these facts, taken as a whole, it is concluded that the sales representatives are independent agents so that none of the company's sales should be apportioned to California.

There are facts present which militate against the status of independent agents, such as the salesman's use of company order forms, devotion of fulltime to sale of the company's products, failure to carry competitive (and, probably, noncompetitive) lines of merchandise, and the use of company-supplied samples. However, they are not deemed sufficient to overcome the facts supporting the conclusion that the sales representatives are independent agents.

Sales are not to be apportioned on the basis of the activity of independent agents but only on the basis of the activity of those having an employer-employee relationship. This position accords with the rules prescribed by the Regulations. Regulation 24301, paragraph (a), under the heading "Sales Factor", provides in part:

The sales or gross receipts factor generally shall be apportioned in accordance with ~~employee~~ sales activity of the taxpayer within and without the State. (Emphasis added.)

The classification of a representative as an employee should ultimately depend on the common-law rules pertaining to the determination of employee and independent contractor. However, a representative will be deemed to be an employee if payroll taxes are deducted from his wages or commissions by his employer pursuant to the Federal Insurance Contributions Act; provided, that either the taxpayer or the Franchise Tax Board, as the case may be, may establish that the sales representative has the status of an independent contractor in the performance of his services. Thus, a sales representative who is being included within the coverage of the Federal Insurance Contributions Act shall be deemed, prima facie, to be an employee; but, nevertheless, it may be shown that inclusion was required by Section 3121(d)(3)(D) of the Act (1954 Internal Revenue Code) and that, for purposes of apportionment of sales, the individual is an independent agent.