COMMONWEALTH OF MASSACHUSETTS

APPELLATE TAX BOARD

SHAKLEE CORPORATION	**v.**	**COMMISSIONER OF REVENUE**
Docket Nos. F245496, F245497		Promulgated: February 7, 2000

These are appeals under the formal procedure pursuant to G.L. c. 62C, § 39, from the refusal of the appellee Commissioner of Revenue ("Commissioner") to abate sales and use taxes assessed for the taxable periods January 1, 1975 through March 31, 1988, and corporate excise assessed for the taxable periods September 30, 1970 through September 30, 1988.

Commissioner Scharaffa heard the appeals and was joined in the decisions for the appellant by Chairman Gurge and Commissioners Burns, Gorton and Egan.

These findings of fact and report are made at the request of the appellee pursuant to G.L. c. 58A, § 13 and 831 CMR 1.32.

John S. Brown, Esq., *Joseph L. Kociubes,* Esq., *George P. Mair,* Esq., *Donald-Bruce Abrams*, Esq., *Darcy A. Ryding*, Esq. and *Matthew D. Schnall*, for the appellant.

Debra S. Rokosz, Esq., *Timothy R. Stille,* Esq. and *Karen L. Paino,* Esq., for the appellee.

FINDINGS OF FACT AND REPORT

Based on the Agreed Statements of Facts, exhibits and witnesses' testimony, the Board found that it had jurisdiction over these appeals and also made the following findings of fact.

During the years at issue Shaklee Corporation ("Shaklee") was a California corporation with its headquarters in San Francisco.[1] At no time during the years at issue was Shaklee qualified to do business in the Commonwealth. Shaklee manufactured and sold a variety of nutritional, household and personal care products. Shaklee distributed its products through independent contractors referred to as "Shaklee Family Members" ("Shaklee Member(s)" or "Member(s)"). The Shaklee products were shipped into the Commonwealth from distribution facilities located outside of the Commonwealth.

During the years at issue, Shaklee had no offices in the Commonwealth and did not own any real or personal property in the Commonwealth.[2] Until 1978, Shaklee had no employees in the Commonwealth. Beginning in that year,

[1] In January 1988, Shaklee transferred its United States operations to a new Delaware subsidiary known as Shaklee U.S., Inc. which continued to operate the same business.

[2] Shaklee did lease vehicles which were used in the Commonwealth as part of the "bonus car program" discussed in more detail below.

Shaklee employed a field relations representative who covered a region that included Massachusetts. On infrequent occasions, the field representative would attend meetings in Massachusetts with “Sales Leaders,” who were Shaklee Members and had achieved a designated sales volume and met certain other requirements, to discuss sales techniques and product information. In addition, for three or four days in 1985, Shaklee held a convention in Boston for qualified Sales Leaders to discuss sales techniques. No Shaklee products were sold and there were no solicitations for orders of Shaklee products at the convention.

To become a Member, an individual had to be sponsored by a current Member, complete an application form, purchase a New Members Information Kit at a nominal charge, and undergo training. The application made it clear that the Member was not to represent, in any manner, that he or she was an agent or employee of Shaklee. Instead, Members were treated as maintaining independent businesses with the right to purchase Shaklee products. Training for new Members was provided by the Member who recruited them. Shaklee did not offer training to new Members nor did it prescribe the method, the content, or the amount of training that was necessary.

By sponsoring new Members, an established Shaklee Member built his or her sponsorship line, the "down line," which extended from the Member down through their new recruits, the individuals they recruited, and so on. Once a Member qualified as a Sales Leader, he or she had to complete another application which clearly noted that the individual was self-employed. The privileges and responsibilities document distributed to the Sales Leaders also stated that Sales Leaders could not imply that they represented or were employees or agents of Shaklee.

Sales Leaders were the individuals who actually purchased the goods from Shaklee. All orders which were submitted to Shaklee had to be accompanied by full payment. Originally, all orders were sent to California for approval by telephone or mail. Later, Shaklee established five distribution facilities outside of Massachusetts where orders were received and filled. Massachusetts Members used the distribution facility in Dayton, New Jersey. Orders were sent there and shipped, via common carrier, to the Sales Leaders.

Once the Sales Leaders received the products from Shaklee, they transferred them to their Members for resale, sold them to their own customer base, kept them for their own use or maintained them as inventory. Members

determined all terms of sale between themselves and their customers including the price, payment by cash or credit, and delivery. If there was an additional delivery charge to get the product to the ultimate customer, the Member bore that responsibility. As part of their customary business practices, Sales Leaders registered as vendors in the Commonwealth and collected and paid to the Commonwealth the appropriate sales tax on their sales to Massachusetts customers.

The business of Members and Sales Leaders was to sell products which the Sales Leaders purchased from Shaklee. Members earned money by purchasing, at a discount, Shaklee products and then reselling them at a higher price. If a Member did a certain volume in a given month, he or she would be paid a bonus.

After a Sales Leader developed his or her business so that there were other Sales Leaders within the group, he or she received “royalties” or “overrides,” based on the group’s monthly sales volume. In addition, Sales Leaders who reached a certain volume of purchases qualified to participate in the “bonus car program” in which Shaklee leased automobiles and sublet them to the Sales Leader as part of an incentive package.

Shaklee imposed no time commitment upon Members or Sales Leaders, who were free to devote as much or as little time to selling Shaklee products as they chose. Also, Shaklee did not require Members to: (1) attend meetings with Shaklee representatives or other Members; (2) file sales or business plans or projections; (3) account for their time; or (4) limit the geographic location of the Member's customer base. Members were free to run their business as they chose. If they maintained a separate office, they were responsible for all associated expenses.

In advertising their business, Members could use a trademarked "Shaklee Independent Distributor" logo, but not Shaklee's corporate trademark or logo. Although Members were responsible for purchasing the samples used in their business, there was no requirement for the amount of purchases. In addition, Shaklee distributorships could be purchased and sold, and passed on following the death of a Sales Leader. Although Shaklee might receive information of the sale, for tracking purposes, it had no knowledge or involvement in the terms and conditions of the sale.

Members had their own customers and were responsible for developing and servicing their customer base. Shaklee put no limits on the size and nature of the Members' organizations. In addition, Members were free to sell both

Shaklee and non-Shaklee products. According to the Sales Leader handbook, the Shaklee policy during the years at issue was that "as independent business persons, you [Sales Leaders] and your Members are responsible for complying with the sales tax laws in all states in which you conduct business." Testimony provided by the Sales Leaders who testified at the hearing of these appeals indicated that as Sales Leaders they did in fact collect and remit the appropriate sales tax to the Commonwealth.

On this basis, and to the extent it is a finding of fact, the Board found that Shaklee's primary activity in the Commonwealth during the years at issue was the solicitation of sales through Members and Sales Leaders. The Board found that the field representatives' occasional visits to the Commonwealth, the Sales Leaders' use of Shaklee owned vehicles and the 1985 Convention were activities entirely ancillary to the solicitation of orders. Furthermore, to the extent that the Convention was not within the realm of solicitation, the Board found that it was a trivial additional connection with the Commonwealth and therefore qualified as a *de minimis* activity for purposes of Public Law 86-272. Accordingly, the Board found that Shaklee was not subject to the corporate excise.

The Board further found that the Members and Sales Leaders who distributed Shaklee products were independent contractors who had no authority to act on behalf of Shaklee with third parties and were not subject to the company's direction and control. Therefore, the Board found and ruled that the Members and Sales Leaders were not Shaklee's "representatives" for purposes of G.L. c. 64H, § 1 and, accordingly, Shaklee was not required to collect the sales/use tax. In addition, the Board further found that the sales taxes at issue had been properly paid by the Sales Leaders, who as a customary practice of their business, collected a sales tax from their customers and remitted it to the Commonwealth. On this basis, the Board issued decisions for the appellant.

OPINION

The two issues in dispute in the present appeal are (1) whether Shaklee was under an obligation to collect and remit to the Commissioner sales and use tax, and (2) whether Shaklee was liable for the corporate excise. Based on the evidence presented, the Board ruled in favor of Shaklee on both issues.

Chapter 64H, § 2 imposes an excise upon "sales at retail of tangible personal property in the commonwealth by

any vendor." There is also imposed an excise upon the "storage, use or other consumption in the commonwealth of tangible personal property [] purchased from any vendor for storage, use or other consumption within the commonwealth." G.L. c. 64I, § 2. The sales tax is imposed upon "[e]very vendor engaged in business in the commonwealth." G.L. c. 64H, § 4. The term "engaged in business in the commonwealth" is defined to include "regularly soliciting orders for the sale of tangible personal property by salesmen, solicitors or representatives in the Commonwealth." G.L. c. 64H, § 1. Because the term "representative" is the broadest of the three categories listed in the definition of "engaged in business" in § 1, if the Members and Sales Leaders were determined to be representatives of Shaklee, Shaklee would have been responsible for collecting and remitting the sales and use taxes at issue in these appeals.

The issue of whether members of a sales force virtually identical to the one at issue in this appeal were "representatives" of an out-of-state corporation for purposes of § 1 was recently addressed by the Board in ***Jafra Cosmetics, Inc. v. Commissioner of Revenue,*** 1999 Mass. A.T.B. Adv. Sh. 650 (Docket No. 178135, November 22, 1999). Jafra Cosmetics was a California-based manufacturer

of cosmetics and skin care products. Jafra sold its products to a sales force, which consisted of consultants, managers and directors, who in turn sold the products to individuals in Massachusetts. The Board found that the company's marketing philosophy was predicated on the consultants' roles as independent retailers. ***Jafra,*** 1999 ATB Adv. Sh. at 653. The Board also found that the sales force did not have authority to act on behalf of Jafra and could not hold themselves out as Jafra representatives. ***Id.*** at 653, 657.

The Board found that the members of Jafra's sales force who were selling Jafra products in Massachusetts were not "representatives" of Jafra but rather were independent contractors. Accordingly, the Board ruled that Jafra's use of independent contractors to solicit sales of Jafra products did not constitute being "engaged in business in the commonwealth" and, therefore, Jafra was not responsible for collecting and remitting the sales tax at issue.

For the same reasons detailed in the Board's opinion in ***Jafra,*** the Board found in the instant appeals that members of the Shaklee sales force were not "representatives" of Shaklee. Therefore, the Board found that Shaklee was not liable for collection of the sales tax. In addition, based on the evidence presented in the

present appeals, the Board found that as part of their normal business operations the individual members of the sales force had collected and remitted to the Commonwealth the applicable sales or use taxes on their respective sales or use of the personal property at issue.

Also at issue in these appeals is whether Shaklee was subject to the corporate excise for tax years 1970 through 1988. Chapter 63, § 39, imposes a corporate excise upon "every foreign corporation . . . actually doing business in the commonwealth . . . in a corporate form."[3] However, Public Law 86-272 (codified at 15 U.S.C. § 381), places a limit on a state's authority to impose a corporate excise where the corporation's activities are limited to the solicitation of orders for sales of tangible personal property, either by an employee or an independent contractor. 15 U.S.C. § 381.

Public Law 86-272 does not define solicitation of orders. However, it is well recognized that solicitation of orders "'covers something more than what is strictly essential to making requests for purchases.'" ***Amgen, Inc. v. Commissioner of Revenue,*** 427 Mass. 357, 360 (1998)

[3] The Board notes that the statute at issue was amended, to its current form, in 1975. The change in the statute, however, has little bearing on these appeals as the federal statute, Public Law 86-272, was in effect at all relevant times and was controlling on the issue of state taxation of an interstate business.

quoting ***Wisconsin Dep't of Revenue v. William Wrigley Jr., Co.,*** 505 U.S. 214, 228 (1992). The only clear line that has been drawn is between those activities that are "entirely ancillary to requests for purchases – those that serve no independent business function . . . and those activities that the company would have reason to engage in anyway but chooses to allocate to its in-state sales force." ***Wrigley,*** 505 U.S. at 228-229.

If a corporation does, however, engage in activities which do not in fact constitute solicitation of orders, such activities may still qualify for the protection of Public Law 86-272 if those activities are *de minimis*. ***Amgen,*** 427 Mass. at 360.

The Commissioner argued that Shaklee exceeded the protected solicitation of orders by virtue of the Sales Leaders (1) accepting returns and issuing refunds; (2) recruiting new Members and requiring them to purchase a new Member kit; (3) qualifying for and participating in the bonus car program; and, (4) maintaining inventory. For the following reasons, the Board found the Commissioner's arguments unpersuasive.

During the years at issue, Shaklee was never qualified to do business in the Commonwealth and never maintained an office in the Commonwealth. Until 1978, Shaklee's only

connection with the Commonwealth was the solicitation of sales of its products through its Members who purchased Shaklee products and in turn sold them to customers. The Sales Leaders sent all orders to either California or New Jersey, where they were filled and shipped back to the Sales Leader, via common carrier. The Board found that the Members were independent contractors, not representatives of Shaklee. Therefore, their activities of selling Shaklee products, accepting returns and issuing refunds, and maintaining an inventory, could not be imputed to Shaklee. Pursuant to Public Law 86-272,

> a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors.

See also 830 CMR 63.39.1(7) ("Activities of an independent contractor will not be imputed to the corporation").

The only physical presence Shaklee had within the Commonwealth was the occasional visits, beginning in 1978, by a field representative and a one-time, three or four day national convention in Boston in 1985. A field representative would occasionally come to Massachusetts to meet with Sales Leaders and to discuss successful sales techniques and product information.

In ***Wrigley,*** the Supreme Court concluded that "in-state recruitment, training, and evaluation of sales representatives . . . served no purpose apart from their role in facilitating solicitation." ***Wrigley,*** 505 U.S. at 234. Accordingly, the Board found that the recruitment of new Members, visits by a Field Representative and the convention to discuss sales techniques were protected activities. The Board also found that the sale of new Member kits, served no independent business purpose apart from soliciting orders and, therefore, was a protected activity. The Court also noted in ***Wrigley*** that a company does not forfeit its tax immunity under Public Law 86-272 by performing some in-state business activities that go beyond "solicitation of orders" if such activities are *de minimis.* ***Wrigley,*** 505 U.S. at 231.

The Court concluded that a particular activity is not *de minimis* if "[it] establishes a nontrivial additional connection with the taxing State." ***Wrigley,*** 505 U.S. at 232. Holding one convention of three- to four-day duration over the course of the 18-year period at issue cannot be regarded as anything other than a trivial additional connection to Massachusetts. Accordingly, to the extent that the convention might have exceeded the mere

solicitation of orders, the Board found that it was only a *de minimis* activity protected by Public Law 86-272.

Lastly, Shaklee's participation in the "bonus car program" was also insufficient to bring it within the sweep of the Massachusetts corporate excise tax. In ***Wrigley,*** the Court concluded that "providing a car . . . to salesmen is part of the 'solicitation of orders' because the only reason to do it is to facilitate requests for purchases." ***Wrigley,*** 505 U.S. at 228. In addition, in Letter Ruling 88-7, the Commissioner concluded that a foreign corporation that owned automobiles which were used by its in-state sales force did not exceed the protections of Public Law 86-272. Similarly, in DOR Directive 88-8, the Commissioner concluded that a corporation's use of personal property, by providing company cars and samples used by its in-state sales force, did not subject it to the corporate excise because the "use made of the property does not exceed the 'solicitation' of orders within the meaning of Public Law 86-272."

Based on the foregoing, the Board found that the Shaklee Members were independent contractors and, therefore, their activities, including soliciting orders, selling Shaklee products, accepting returns and issuing refunds, as well as recruiting new members, were not

attributable to Shaklee. Furthermore, the Board found that the visits by a field representative, the 1985 convention, the recruiting of new Members, the sale of new Member kits and the use of company leased vehicles were within the meaning of "solicitation of orders" as intended by Public Law 86-272. Lastly, to the extent that the convention held in 1985 might have been found to exceed "solicitation," it was simply a *de minimis* activity that did not remove the protections afforded by Public Law 86-272.

Accordingly, the Board issued a decision for the appellant and granted abatements in the amount of $214,163 for corporate excise and $2,190,041 for sales tax.

APPELLATE TAX BOARD

By:_____
Frank J. Scharaffa,
Acting Chairman

A true copy,

Attest:_____
Clerk of the Board