

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petitions	:	
of	:	
ATN MARTS, INC.	:	DECISION
AND 24 OTHER PROCEEDINGS	:	
for Review of a Denial, Suspension, Cancel-	:	
lation or Revocation of a License, Permit or	:	
Registration under Article 20-A of the Tax Law.	:	

Petitioners ATN Marts, Inc. and 24 other petitioners (hereinafter "petitioners") filed an exception to the determination of the Administrative Law Judge concerning their petition for review of a denial, suspension, cancellation or revocation of a license, permit or registration under Article 20-A of the Tax Law (File No. 806214). Petitioners appeared by Hodgson, Russ, Andrews, Woods & Goodyear (Paul R. Comeau, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq., (E. Roger Jenkins, Esq., of counsel).

Both parties submitted briefs on exception. Oral argument, at the request of petitioners, was heard on July 18, 1989.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUES

I. Whether the Division of Taxation properly refused to register petitioners as a chain store pursuant to Article 20-A of the Tax Law.

II. Whether petitioners' motion to strike the Division's Memorandum of Law filed in response to the petitioners' exception should be granted on the grounds that a) it does not address the issues raised in petitioners' exception and b) it is in the nature of a cross exception in that it seeks to raise issues with respect to the determination of the Administrative Law Judge which are not the subject of the petitioners' exception to the Tribunal.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge and such facts are restated below¹. We also find additional facts as indicated below.

Chain stores which have been registered by the Department of Taxation and Finance are permitted by law to purchase cigarettes from wholesale dealers at the chain store price, which is less than the price otherwise paid by retailers.

With the exception of Convenience Corner and Pine Valley Busy Mart, petitioners² are members of Target Cooperative Buying Association, Inc. ("Target"), a New York corporation, incorporated on February 2, 1988, pursuant to Article 2 of the New York Cooperative Corporations Law.

Target has filed its certificate of incorporation with the Secretary of State and has filed both its certificate of incorporation and bylaws with the Department of Agriculture and Markets, as required by section 15 of the Cooperative Corporations Law.

Target's certificate of incorporation and bylaws, in form, conform to the requirements of sections 11 and 16 of the Cooperative Corporations Law.

Target's corporate purposes, as listed in the certificate of incorporation, are permitted purposes under subdivision 2 of section 11 of the Cooperative Corporations Law.

Petitioners sell cigarettes at retail through 15 or more separate establishments in New York State.

Each petitioner, with the exception of Convenience Corner, Pine Valley Busy Mart, Kerr's Pick Quick Food Mart, Mike's Quick Stop and Rosati IGA Market, submitted an application for a certificate of registration as a chain store pursuant to article 20-A of the Tax Law.

¹At hearing, petitioners and the Division of Taxation stipulated to seven facts and to the introduction into evidence of certain documents. The stipulated facts have been incorporated herein.

²Petitioners are identified in Appendix I.

On or about March 29, 1988, the [Division of Taxation] of the State of New York Department of Taxation and Finance mailed to each petitioner a Notice of Proposed Refusal to Register as a Chain Store, on the ground that "[Target] does not qualify under the Cigarette Marketing Standards Act."

On or about September 8, 1988, the [Division of Taxation] mailed to each petitioner a revised notice of proposed refusal to register as a chain store, and each such notice stated that the refusal was based on the [Division's] conclusion that: "The purposes of [Target] are not within section 13 of Cooperative Corporations Law."

Each application at issue here indicated that the applicant met the statutory definition of a "chain store" by virtue of being a cooperative member, and attached to each application was a Target membership certificate. Each applicant listed Tripifoods, Inc. as a major supplier of its cigarettes.

Tripifoods is a cigarette wholesale dealer and a regional wholesale supplier of groceries and other consumer items to retail establishments.

Upon receipt of the first of the applications at issue, the Division of Taxation ("Division") attempted to verify that Target was registered with the Department of Agriculture and Markets, as required by the Cooperative Corporations Law. While awaiting the result of this inquiry, the Division received several telephone calls from members of the cigarette industry, claiming that Target did not qualify as a cooperative under article 20-A of the Tax Law. Shortly thereafter, the Division determined that Target was incorporated under the Cooperative Corporations Law and registered with the Department of Agriculture and Markets. The Division then requested, and received, copies of Target's certificate of incorporation, bylaws and membership agreement.

Target's certificate of incorporation states its purposes as follows:

"The corporation is formed under and pursuant to the provisions of Article 2 of the Cooperative Corporations Law, and its objects and purposes are such as are authorized for general cooperative corporations under such Law, to wit:

"To assist its members, or any of them, by performing services connected with the purchasing, financing, producing, manufacturing, warehousing, preserving, processing, packing,

grading, storing, handling, shipping, marketing, merchandising or selling of the agricultural and food products of its members or any by-products thereof, or connected with the acquisition for its members of labor, supplies and articles of common use."

Target's incorporators are shown as Anthony L. Dutton, Pamela D. Heilman, Terry C. Burton, Bonnie A. Redder and Michael A. O. de Freitas. Each incorporator's address is shown as 1800 One M & T Plaza, Buffalo, New York. None of the incorporators are members of Target.

The names of Target's directors are shown as Robert E. Hilburger, G. Ronald Dixon, R. Sterling Cole, Joan A. Foster and Anthony D. Rano. Each director's address is shown as 1427 William Street, Buffalo, New York.

Robert E. Hilburger and G. Ronald Dixon are officers of Tripifoods; Tripifoods' business location is 1427 William Street, Buffalo, New York.

Target's bylaws contain the following provisions:

(a) Membership in Target is restricted to individuals, partnerships, corporations and other business entities "which are engaged in the retail grocery store business".

(b) Target's board of directors is granted the right to terminate, upon 30 days' notice, a member's membership in Target for any reason or no reason.

(c) Each member is entitled at every meeting to one vote on all matters appropriate for consideration by the membership, and each member may authorize another person or persons to vote by proxy.

(d) The affairs of Target are to be managed by the board of directors.

(e) Each of the directors must be a member of Target or an officer of a partnership, corporation or other business entity which is a Target member.

(f) Any member may bring charges against a director by filing them in writing with the Secretary of Target, together with a petition for removal signed by 5% of the membership. A director may be removed by "the affirmative vote of three-fourths of the members voting thereon at a meeting promptly held after due notice in writing setting forth the purpose for which such meeting is called, provided that at such meeting not less than 10% of the entire membership vote, personally or by mail."

(g) Any director may be removed for cause by a majority vote of the entire board.

(h) Vacancies occurring on the board of directors may be filled by a vote of a majority of the directors then in office, even where no quorum exists, or by vote of the members at any meeting where members have been put on notice of the proposed election. Unless elected by the members, a director elected to fill a vacancy shall serve until the next meeting of members at which the election of directors is in the regular order of business.

(i) Target's board of directors may appoint a three-member Executive Committee from among its members, and such committee shall have all authority of the board of directors in the interim between meetings of the board of directors.

(j) Target's board of directors may annually appoint or elect a president, one or more vice presidents, a secretary or treasurer. The president and vice president must be members of Target or a representative of a member and shall be appointed from among the directors. The president of the board shall be the chief executive officer of Target.

Target's initial membership application and agreement contained these provisions:

"2. Effective upon the acceptance of the Applicant's membership in the Cooperative, the Applicant appoints the Cooperative as the agent of the Applicant, and the Cooperative accepts such appointment, for the purpose of procuring and purchasing for the Applicant certain merchandise, products and other commodities as are necessary or useful in the conduct of the Applicant's business. No purchase shall be made by the Cooperative for or on behalf of the Applicant pursuant to the foregoing agency relationship unless the Applicant makes a specific request. The Applicant is solely responsible to make payment in full, directly to the seller for such merchandise, products and other commodities.

3. The Applicant understands that Tripifoods, Inc. has agreed to provide management of the Cooperative at no cost to its members, other than reimbursement of reasonable expenses incurred in providing such management. In consideration of such service, the Applicant hereby agrees to execute the proxy attached hereto and made a part hereof, intending that this Agreement be construed as a voting agreement for purposes of section 620(a) of the New York Business Corporation Law."

The proxy referred to in the second quoted paragraph is an irrevocable proxy. It states, in pertinent part:

"On any vote for the election of directors of Target Cooperative Buying Assn., Inc. (the 'Cooperative'), the undersigned hereby constitutes and appoints the President or any Vice President of Tripifoods, Inc. as the true attorney, agent and proxy of the undersigned to vote at any meeting of the members of the Cooperative as follows: (a) on any vote for the election of the Board of Directors of the Cooperative, for five individuals nominated by Tripifoods, Inc. or its successor or assignee, (b) on any vote for the removal of any director of the Cooperative, as directed by Tripifoods, Inc. or its successors or assignee, and (c) on any vote to fill a vacancy on the board of directors of the Cooperative arising from the death, inability to serve, resignation or removal of any director, for a person nominated by Tripifoods, Inc. or its successor or assignee."

The first meeting of Target's board of directors was held on February 6, 1988. The board unanimously adopted the following resolution:

"Resolved, that the proposed Membership Application and Agreement and Irrevocable Proxy presented to this meeting be, and it hereby is, approved and adopted as the form of membership agreement to be entered into between the corporation and Tripifoods, Inc. and each of the proposed members of the corporation."

By letter dated March 25, 1988, the Division advised Target's lawyers that "notwithstanding certain facial indicia of cooperative corporation status", the Division's review of Target's bylaws, membership application and irrevocable proxy indicated "that Target will not operate as a cooperative corporation as defined by section 3(c) of the Cooperative Corporations Law, and therefore, its members may not register as 'chain stores' by reason of their membership in Target." The Division's determination that Target would not operate as a cooperative corporation was based primarily on its conclusion that Target's board of directors would be completely controlled by Tripifoods which would thereby be able to operate Target for its own economic self-interest, rather than for the benefit of Target's members.

The Division issued notices of proposed refusal to register as a chain store to all Target members who had submitted applications, but despite this, discussions continued between the Division and Target's attorneys, regarding the Division's decision.

In response to the concerns stated in the Division's March 25th letter, Target revised its membership application and agreement by eliminating paragraph three of the application and with it the requirement that all members execute an irrevocable proxy in favor of Tripifoods. Each Target member executed a notice of termination cancelling its existing membership application and agreement and irrevocable proxy statement. Each then executed the new membership application and agreement.

Revised Target membership applications and agreements were forwarded to the Division for all petitioners except Convenience Corner and Pine Valley Busy Market.

The Division issued revised notices of proposed refusal to register as a chain store, dated September 8, 1988, to all petitioners from whom it had received the revised Target membership application and agreement. The notice stated:

"Notwithstanding your Notice of Termination and subsequent new membership application and agreement with Target Cooperative Buying Association (the 'cooperative'), the purposes of the cooperative are not within section 13 of the Cooperative Corporation Law."

We find additionally that an Opinion of Counsel (Exhibit O) dated September 8, 1988, addressed to petitioners' representatives indicated that the basis for such proposed action is "... our belief that section 13 of the Cooperative Corporations Law, which sets forth the purposes for which a cooperative corporation may be formed, does not envision the formation of a cooperative corporation for the purpose of acquiring cigarettes and other commodities for its members, for their resale to the public through the members' individual retail stores."

The impetus for Target's formation came from retail stores seeking to take advantage of the chain store provision of article 20-A of the Tax Law. One of these businesses is petitioner MWS Enterprises, Inc., whose president, Mark Sidebottom, testified at hearing. Mr. Sidebottom and other retailers contacted Tripifoods to ask if a mechanism could be found that would allow them to qualify as chain stores under article 20-A. Tripifoods agreed to research their inquiries, and Target was the result.

Target was organized by Tripifoods which prepared Target's certificate of incorporation, bylaws and membership agreement, undertook all activities necessary to incorporate Target and provided administrative and support services to Target.

Target has a membership of approximately 70 and a membership goal of 200. Each member paid an initial fee of \$50.00 which was intended to fund the corporation. There is no evidence that any member was ever actively involved in Target's formation.

Target is not operational. It has no business office, business telephone or other property. There has never been a membership meeting. Target has made no purchases, and its members have made no purchases through it. Mr. Sidebottom stated that it is not operational because the members are awaiting the outcome of their efforts to register as chain stores.

Target was formed solely for the purpose of enabling its members to register as chain stores under article 20-A of the Tax Law.

OPINION

Article 20-A of the Tax Law, commonly referred to as the Cigarette Marketing Standards Act (CMSA) was adopted by the Legislature in 1985 (L 1985, ch 897, effective September 1, 1985). CMSA established minimum percentage markups to be used by wholesale dealers and retailers in determining the minimum price of cigarettes (Tax Law § 483) and made it illegal for wholesale dealers and retailers to sell cigarettes in New York State at less than the minimum price (Tax Law § 484[a]).

The "basic cost of cigarettes", to which the wholesale dealer's markup was to be applied, was defined as the invoice cost of cigarettes to the wholesale dealer, or the replacement cost of cigarettes to the wholesale dealer, in the quantity last purchased, whichever is lower, with certain other adjustments (Tax Law § 483[a][11]).

CMSA treated chain stores as wholesale dealers for purposes of their purchases of cigarettes from wholesale dealers and as retail dealers for purposes of their sales of cigarettes to consumers (Tax Law § 484[a][2] and [4]). Thus, retail dealers qualifying as chain stores enjoyed a competitive advantage over retailers who did not so qualify since they were able to purchase

cigarettes from wholesalers at a lower price than retail dealers who did not qualify as chain stores.

As originally enacted, a chain store was defined as:

" . . . any person or persons who owns or maintains fifteen or more retail outlets. . . by the maintenance of an established place of business for the purchase of cigarettes, including, but not limited to, the maintenance of warehousing facilities for the storage and distribution of cigarettes." (Tax Law § 483[a][3].)

CMSA was criticized by smaller retailers and "subjobbers" (i.e., non-agent wholesalers) who complained that the chain store provision unfairly favored large retail chains over other retailers.³ Chapter 860 of the Laws of 1987 attempted to address the perceived inequities of CMSA, in part, by allowing more retailers to qualify as "chain stores" (Governor's Memorandum of Approval of Chapter 860 of the Laws of 1987 [December 23, 1987] Governor's Bill Jacket, supra).

Tax Law section 483(a)(3), as amended by Chapter 860, defines a chain store as:

" . . . any person or persons who owns or maintains fifteen or more retail outlets in New York state, having one hundred percent common ownership, through which cigarettes are sold at retail. Vending machine operators who sell cigarettes at not less than fifteen separate outlets shall be considered to be chain stores. It shall also include cooperative members, franchisees and large volume outlets." (Emphasis added.)

Tax Law section 483(a)(5) states:

"'Cooperative member' shall mean any member of a 'cooperative' as defined in subdivision (c) of section three of the cooperative corporations law, whose members sell cigarettes at retail through fifteen or more separate establishments in New York state."

Section 3(c) of the Cooperative Corporations Law provides, in part:

"The terms 'cooperative,' 'cooperative association' and 'cooperative corporation' mean a corporation organized under this chapter, . . . for the cooperative rendering of mutual help and service to its members." (Emphasis added.)

Section 3(d) of the Cooperative Corporations Law provides:

³Letter from Roderick G.W. Chu, Commissioner of Taxation and Finance, to the Honorable Mario M. Cuomo (July 17, 1987), Governor's Bill Jacket, L 1987, ch 860.

"A cooperative corporation shall be classed as a non-profit corporation, since its primary objective is not to make profits for itself as such, or to pay dividends on invested capital, but to provide service and means whereby its members may have the economic advantage of cooperative action, including a reasonable and fair return for their product and service." (Emphasis added.)

All chain stores, including individual cooperative members, are required to register with the Commissioner and to provide such information as the Commissioner, by regulation or instruction, may require (Tax Law § 489). To the extent that they can be made applicable, the licensing provisions of the Tax Law section 480 are applicable to the registration of chain stores (Tax Law § 489).

The Administrative Law Judge determined that a) the Division was authorized to refuse to register petitioners based on its interpretation of the Cooperative Corporations Law, b) cooperatives, such as Target, can be formed for the purpose of purchasing goods for resale to the public and that the Division's refusal to register petitioners on such ground was not valid, and c) the sole purpose for the creation of Target was to allow its members (e.g., petitioners) to take advantage of the chain store provisions of CMSA. Accordingly, the Administrative Law Judge determined that Target was not a cooperative within the meaning of the Cooperative Corporations Law since its prime purpose was for economic advantage of its members and not "... for the cooperative rendering of mutual help of its members" as provided by Cooperative Corporations Law section 3(c). The Administrative Law Judge sustained the Division's refusal to register the petitioners solely on this ground.

On exception, the petitioners assert that Target was not formed solely for the purpose of taking advantage of the chain store provisions of CMSA, that it is a cooperative as that term is defined in section 3(c) of the Cooperative Corporations Law, and that in determining to the contrary the Administrative Law Judge exceeded her jurisdiction, since the issue upon which the Administrative Law Judge based her determination was not specifically asserted by the Division as a grounds for denial, and was not raised by either party at hearing. Petitioners assert that Target and its members satisfy the "cooperative action" test upon which the Administrative Law Judge based her determination, and further, that Target is a cooperative corporation under section

3(c) of the Cooperative Corporations Law. In addition, petitioners have filed a motion to strike the Division's Memorandum of Law submitted in response to petitioners' exception on the ground that, in reality, it is a cross exception.

In response to the petitioners' exception, the Division concedes that a cooperative can be formed solely for the purposes of the CMSA. However, the Division asserts that a) Target was not formed by its members for their mutual help but was formed by Tripifoods, Inc. as a marketing mechanism to carry out its corporate business purposes, b) the refusal to register petitioners was a reasonable interpretation of legislative intent and within the authority of the Division as the licensing authority, and c) all proper inferences should be drawn from the refusal of the President of Tripifoods to testify at the hearing.

We agree with the determination of the Administrative Law Judge that the Division was authorized to interpret the Cooperative Corporations Law in its analysis of petitioners' applications, that cooperatives can be formed for the purpose of purchasing goods for resale to the public and that the Division's refusal to register petitioners on such ground was not proper and that the sole purpose for the creation of Target was to take advantage of CMSA.

We reverse the determination of the Administrative Law Judge solely with respect to that portion of the determination concluding that Target was not a cooperative for purposes of the Cooperative Corporations Law section 3(c) because it was formed primarily for the economic advantage of its members.

We deal first with petitioners' motion to strike the Division's Memorandum of Law. In our opinion, the Memorandum of Law deals with the substance of the issues in this case and does not raise new issues which would only properly be raised by the filing of an exception. Accordingly, the motion is denied.

We deal next with the Administrative Law Judge's determination that Target is not a cooperative within the meaning of the Cooperative Corporations Law because it was formed solely for the purpose of enabling its membership to take advantage of the chain store provisions of CMSA. More particularly, the Administrative Law Judge concluded:

"However, the hallmark of a cooperative is not so much economic advantage as it is 'cooperative action'. A cooperative formed for the purpose of qualifying its members as chain stores is not formed 'for the cooperative rendering of mutual help and service to its members' (Cooperative Corporations Law § 3[c]), but to take advantage of CMSA. It is concluded, therefore, that a corporation formed solely to take advantage of the chain store provisions of CMSA is not a cooperative as defined by section 3(c) of the Cooperative Corporations Law."

We find this conclusion inconsistent with the specific language of the 1987 amendments to the CMSA and section 3(d) of the Cooperative Corporations Law which provides in part that the "primary objective [of a cooperative corporation] is . . . to provide service and means whereby its members may have the economic advantage of cooperative action, including a reasonable and fair return for their product and service." (Emphasis added.)

The amendments to CMSA were made to enable additional retailers to take advantage of the pricing structure contained in CMSA. The benefit to be extended was clearly economic in nature, i.e., a higher profit margin on the sale of cigarettes. The language used to extend this benefit is straightforward and clear, namely, cooperative members, franchisees and large volume outlets (Tax Law § 483[3]).

"Cooperative member" means a member of a cooperative as defined in subdivision (c) of section three of the cooperative corporations law, whose members sell cigarettes at retail through fifteen or more separate establishments in New York State. (Tax Law § 483[5].) Section 3(d), as we have noted, envisions the primary object of a cooperative as providing "economic advantage" for its members including a reasonable and fair return for their product and service.

Clearly, the ability of Target's members to qualify as chain stores for purposes of CMSA is a benefit not available to any of them acting individually. It is only through the cooperative action of the members leading to the creation of Target that each becomes entitled to the benefit accorded chain stores under CMSA. We find nothing in the record here which indicates that this type of cooperative action is not within the purview of Cooperative Corporations Law section 3(c).

According, it is ORDERED, ADJUDGED and DECREED that:

1. The exceptions of ATN Marts, Inc. and the 24 other petitioners are granted;
2. The determination of the Administrative Law Judge is reversed; and
3. The petitions of ATN Marts, Inc. and the 24 other petitioners are granted.

DATED: Troy, New York
August 24, 1989

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner

/s/Maria T. Jones
Maria T. Jones
Commissioner