

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petitions	:	
of	:	
HAMMACHER SCHLEMMER CO., INC.	:	DECISION
for Revision of a Determination or for Refund of Sales and	:	DTA NO. 816215
Use Taxes under Articles 28 and 29 of the Tax Law for the	:	AND 816216
Period December 1, 1990 through February 28, 1997.	:	

Petitioner Hammacher Schlemmer Co., Inc., 303 W. Erie Street, 6th Floor, Chicago, Illinois 60610, and the Division of Taxation each filed an exception to the determination of the Administrative Law Judge issued on December 16, 1999. Petitioner appeared by Jenner & Block (David J. Bradford, Esq., of counsel). The Division of Taxation appeared by Barbara G. Billet, Esq. (Patricia O. Kahn, Esq., of counsel).

Petitioner filed a brief in support of its exception and in opposition to the Division of Taxation's exception. The Division of Taxation also filed a brief in support of its exception and in opposition to petitioner's exception. Oral argument was not requested.

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

ISSUES

I. Whether the imposition of use tax on the cost of printing petitioner's catalogues violated the First Amendment or the Commerce Clause of the United States Constitution.

II. Whether the mailing of catalogues into New York State from outside of the State constituted a “use within the State” within the meaning of Tax Law §§ 1101(b)(7) and 1110.

III. Whether petitioner is entitled to a refund on the portion of the tax which was based on the distribution of catalogues in New York City.

IV. Whether it was proper for the Division of Taxation to impose use tax on the cost of printing petitioner’s catalogues in Tennessee.

V. Whether a finding that petitioner’s publications were “catalogues” precludes consideration of whether they were periodicals entitled to exemption from sales and use tax pursuant to Tax Law § 1115(a)(5).

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

During the years in issue, petitioner, Hammacher Schlemmer Co., Inc. (“HSC”), was a company which sold products through a catalogue and at retail locations. HSC also advertised in Blue Sky which is an airline in-flight catalogue that featured many different catalogues. HSC’s corporate headquarters were in Chicago, Illinois and all of HSC’s corporate executives maintained their offices in Illinois.

Background

The Division of Taxation (“Division”) conducted a sales and use tax audit of HSC for the period December 1, 1990 through November 30, 1993. To the extent in issue, the Division concluded that petitioner distributed catalogues in New York and that tax was due on the paper and printing charges incurred to create the catalogues. Consequently, HSC was assessed

\$298,587.54 in New York use tax for catalogues delivered into New York plus interest in the amount of \$81,330.82 for the period December 1, 1990 through November 30, 1993. Petitioner paid the tax and interest and filed a claim for refund which was denied on August 20, 1996.

On November 6, 1996, HSC requested a conciliation conference. The conciliation conference was held on August 5, 1997 and in an order dated September 26, 1997, the conciliation conferee denied the request for a refund. On November 17, 1997, petitioner filed a petition with the Division of Tax Appeals.

HSC was also audited for the period March 1, 1994 through May 31, 1995. As a result, HSC was assessed an additional \$80,217.92 of New York use tax plus interest of \$17,447.19 for catalogues shipped to New York residents. HSC remitted the additional tax plus interest.

HSC purchased a printing service and paper. These were the two items which comprised the cost of the catalogues for the audits. Approximately 40 percent of the use tax assessments was based on the cost of printing and approximately 60 percent of the use tax assessments was based on the cost of the paper.

In order to avoid potential future use tax liability, HSC voluntarily remitted use tax of \$120,121.90 for the period February 1994 through February 1997.

In June 1997, HSC filed a claim for refund for such amounts, totaling \$217,787.01 ($\$80,217.92 + \$17,447.19 + \$120,121.90 = \$217,787.01$). On August 28, 1997, this claim was denied. Petitioner did not request a conciliation conference. Instead, a petition to the New York State Division of Tax Appeals was filed on November 17, 1997 along with a request to consolidate the cases.

Petitioner collected and remitted New York State sales tax on catalogue sales which were shipped to New York customers.

HSC's Corporate Headquarters

As noted, HSC's corporate headquarters and all of its corporate executives were located in Chicago. None of HSC's corporate decisions were made in New York. It employed, in total, from 150 to 300 employees annually depending upon the season. Of the total number of people employed, approximately 70 people worked in Chicago.

Petitioner's product buyers were all located in its Chicago corporate offices. In determining what products should be included in the catalogue, HSC's product buyers reviewed samples which were sent to them or that they saw at trade shows or in trade publications. The product buyers evaluated the product and determined whether the item met HSC's overall criteria for inclusion in the catalogue.

HSC's primary purpose was to offer its customers only the best and unexpected in product line. Its mission was to ensure that the products selected for inclusion in the catalogue were either the very best of their kind or provided some kind of unique or unusual feature that no other product provided.

Generally, after the buyers identified possible products for inclusion in the catalogue, the products were sent to the Hammacher Schlemmer Institute ("Institute") which was located in Chicago. The Institute, which employed four or five individuals, was an independent research group which performed market research on products offered by HSC and rated those products in comparison to other products. It used customer panelists as well as other outside sources to test and rate products and to inform the Institute which products were best in their particular

category. The Institute performed testing only for HSC. It paid its expenses from funds received from HSC. HSC determined how much money would go to the Institute on the basis of the cost of operating the Institute. None of the Institute's employees were located in New York.

The Institute was a separate and distinct legal entity from HSC. However, the Institute and HSC had the same shareholders. According to the controller of HSC, it was organized as a not-for-profit corporation under the laws of the State of Illinois. The Institute filed a U.S. Corporation Income Tax Return for Subchapter S Corporations (Form 1120S) with the Internal Revenue Service.

After products were selected for inclusion in the catalogue, HSC's buyers and creative staff started assembling the catalogue based upon the selections made by the Institute. Neither the buyers nor the creative staff were located in New York.

HSC's buyers in Chicago negotiated with vendors for a price for purchasing the product. When the product was initially purchased, HSC maintained physical possession of the product in Chicago. If needed, the product was turned over to the rebuying staff in Chicago for further purchasing. None of the rebuying staff was located in New York.

HSC's Catalogue

Once the product was purchased, the product, product literature, and any test result from the Institute and any comments from the buyers were passed on to HSC's creative or advertising departments to prepare the pictorials and the written copy for the catalogue. HSC's copy-writing staff prepared and submitted copy for the catalogue based upon product literature, the buyers' comments and the Institute's tests and comments.

HSC's copy staff and production staff were located in Chicago.

HSC maintained its inventory of catalogue products in Ohio. Although the retail stores would occasionally order merchandise directly from vendors, most of the inventory sold by the retail stores was obtained from the Ohio facility. HSC employed approximately 50 to 200 people in Ohio, depending upon the season.

The following statement contained on page one of HSC's catalogue for Winter 1991 referred to HSC's primary mission as well as its tradition: "Offering the Best, the Only, the Unexpected for Over 149 years." The statement "the best" referred to those products that the Institute had selected through its testing results as the "best" in a particular category. The statement "the only" referred to products that were generally not otherwise available and the statement "the unexpected" referred to a unique product that could not be found in normal product selections through the marketplace.

Petitioner's Winter 1996 catalogue contained the following historical statement relating to HSC:

During the 1930's and 40's, the name Hammacher Schlemmer would become synonymous with innovation. We introduced the first pop-up toaster (1930), the electric razor (1934) and the first steam iron (1948). Later, we would offer the first electric pencil sharpener, food processor, electric can opener and automatic coffee maker [;] the first microwave oven (1968), telephone answering machine (1968) and cordless telephone (1975). At their introduction, these products were viewed by many as intriguing gadgets, we saw them as functional problem solvers. (Hammacher Schlemmer Co., Inc. Catalogue, Winter 1996, p.2.)

All text and product photographs contained in the catalogue were prepared in Chicago. New York personnel were not involved in either the preparation of the text or product photographs for the catalogue.

After the text and product photographs to be set forth in the catalogue were prepared, the catalogue layout and design were created and placed on a computer system. This process took place in Chicago. New York staff were not involved in this process.

The film for the catalogue was created in either Chicago, Illinois or Milwaukee, Wisconsin in preparation for the printing of the catalogues. HSC's production staff arranged for the creation of the film. New York personnel were not involved in the creation of the film or any aspects of ordering the film. After the film was procured from either Chicago or Milwaukee, it was sent to HSC's printer, World Color Press, located in Tennessee.

A typical catalogue during the audit period did not contain an index to articles. There were pages with product pictures, descriptions, item numbers and prices. A review of the catalogues in the record shows that HSC did not make a practice of comparing competing products that were not sold in the catalogue. Many catalogues contained little prose except product descriptions. The catalogues contained order forms and solicited orders.

The following is a representative product description from the Winter 1996 Hammacher Schlemmer Co., Inc. catalogue:

THE ONLY SELF-RIGHTING WALKING CANE.

Winner of the Grand Prize in the 1995 Hammacher Schlemmer Search for Invention competition and featured in the *Journal of the American Medical Association*, this walking cane returns itself back to an upright, vertical position anytime it is dropped or knocked over. Weighing just over one pound, its patented design incorporates a curved, wire-cage base that relies on the force of gravity to always return the cane to an upright stance (in much the same way that a child's inflatable punching bag does). Its sturdy shaft and handle are made from a lightweight, graphite epoxy composite material, the same used in high performance aircraft. The ergonomically designed handle grip is made of flexible black foam rubber for comfort. The seven-inch diameter base was

designed to easily clear the user's foot and is made from metal and rubber components. Shaft is rosewood colored; base has a black finish. Available in 30-, 32-, 34- and 36-inch lengths - please specify.

62321X.....\$99.95

Printing and Mailing of the Catalogues

HSC printed catalogues approximately 14 times a year, including two printings, with different covers, of each of the four seasonal editions, i.e., winter, spring, summer and fall editions. In addition, a holiday catalogue was produced and other catalogue mailings might be done periodically. Approximately 30 million catalogues were distributed annually. There were approximately 100,000 new annual registrations for catalogues. Thus, the new registrants would receive in total 1,400,000 catalogues over the course of a year (100,000 x 14 catalogues each year). Approximately 9,000 of the 100,000 new annual subscribers resided in New York. The balance of the 30 million catalogues which were distributed each year were sent to those who were already on the mailing list.

Recurring customers who were already on the mailing list did not have to pay a subscription fee. With respect to new customers, the advertisements in the record show that sometimes the catalogues were offered for free. In another instance, there was a charge of \$3.00 for the catalogue but the customer received a \$3.00 credit toward a purchase. In other instances there was a charge of \$2.00 or \$3.00 for a full-year subscription. HSC offered subscriptions to its catalogue by, among other things, advertising the subscriptions in other publications. Petitioner has advertised for subscriptions to its catalogue in, by way of example, the Smithsonian, the New Yorker, Town and Country and Harpers Magazine. HSC has advertised its subscriptions as "It's a classic. It's one of a kind."

Petitioner made a small percentage of its total distribution of catalogues available for free to customers of the New York retail store. Approximately two one-hundredths of one percent of the total distribution of the catalogues were distributed in this manner.

The catalogue was not available at newsstands but was available for circulation to the public.

The ultimate purpose of the catalogue was to have customers purchase the products advertised therein. Petitioner has found that putting the "best" rating next to a product results in a more favorable response.

HSC's marketing staff, which was located in Chicago, decided who was to receive the catalogue. It created the mailing list for the catalogue out of HSC's customer computer database. The computer database, from which the mailing list was created, was located in Chicago. Petitioner drew its customer database from the following sources. (1) Customers at the retail stores (New York, Chicago, Beverly Hills) could request that they be placed on a mailing list. The customer's information could be taken on a piece of paper at the store by the clerk or the information could be placed on a card furnished by the store that the customer could send in the mail. (2) The store would obtain the name and address of those customers which asked that a product be shipped. (3) Customers that acquired petitioner's 800 number could call and register to receive the catalogue. That number could be obtained from other catalogues or from ads which were placed in magazines. (4) Customers that previously made purchases over a specified period of time would be included in the mailing database. (5) Customers may have been on the list from prior purchasing history. (6) Petitioner rents mailing lists. New York personnel were not involved in any of the decisions regarding the mailing list for the catalogue. HSC's staff in

Chicago determined the number of copies of the catalogue the printer would print; no New York personnel were involved in these decisions. The mailing list and information regarding the number of copies to be printed were then sent to the printer.

From 1992 through the end of the audit period, all of HSC's catalogues were printed by World Color Press in Dyersburg, Tennessee. Prior thereto, all of HSC's catalogues were printed by R. R. Donnelly & Co. in Mattoon, Illinois. The printers affixed the qualified names and addresses to the catalogues at its facilities in Tennessee and Illinois. All affixation of names and addresses to the catalogues was done by the printer at its facilities in Illinois and Tennessee. The catalogue provided that it would be delivered to the identified recipient or the current resident. World Color Press in Dyersburg, Tennessee also performed a mailing qualification which is a postal rate qualification.

Petitioner's catalogues were mailed third class mail because that is the U.S. postal service mailing class for catalogues. Second class mailing was not used because that is the class for periodicals.

New York employees did not have any involvement with the activities or functions of the printer. They did not have any communication with the printer. HSC contracted for the printing and distribution of the catalogues from its Illinois headquarters. HSC's New York operations did not have anything to do with the distribution of the catalogue. HSC did not engage in any activities within the State of New York related to the production or distribution of the catalogue. HSC's employees did not enter New York State to distribute or otherwise make arrangements for the distribution of the catalogues. No employees with responsibility for catalogue operations worked in New York.

World Color Press obtained the paper used in the production of the catalogue from a paper broker located in Chicago. HSC's production staff in Chicago communicated with the paper broker who procured the paper and sent it directly to HSC's printer in Tennessee. The paper, as well as the printer's services, was paid for out of HSC's accounts payable department in Chicago.

HSC's New York employees did not have any involvement in the paper procurement process, or the payment for the paper or printer.

After the catalogues were printed, the printer prepared the catalogues in bundles for distribution to the various regional or sectional centers of the postal service for final distribution. The catalogues were bundled with catalogues from other companies in order to achieve a better postal and shipping rate. HSC's Tennessee printer determined how the catalogues were to be bundled. The printer transported the labeled catalogues to the United States Postal Service outside of New York. The bundles from World Color Press were weighed at the post office in Tennessee to determine the amount of postage. The postage was then paid in Tennessee.

After the bundles were weighed and the postage was paid, the bundles from World Color Press were placed on skids, the skids placed on trucks, and the trucks sealed in Tennessee. Once the trucks were sealed in Tennessee, HSC could not change the composition of the bundles. Further, at this juncture, HSC had no right or ability to further direct where the catalogues would go or what would happen to them. Neither HSC nor the printer authorized the return of undeliverable catalogues and if a catalogue was deemed "undeliverable" by the Postal Service, the catalogue was not returned to HSC.

Upon delivery of the catalogues to a United States Post Office, neither HSC nor its printers withdrew the catalogues from the United States mails or otherwise redirected the catalogues.

HSC could not and did not retrieve its catalogues from the United States mail. Any catalogues distributed in New York were distributed through the United States mail originating outside of New York.

Customers who wished to purchase a product from the catalogue dialed an 800 number which corresponded to an HSC call center located in Ohio. The customer placed his or her order with the customer representative located in Ohio. The customer representative answered any questions about the ordering process and placed the customer's order into the computer system located in Ohio. The products were then shipped from Ohio directly to the customer.

All decisions regarding HSC's catalogues were made in Illinois, including content of the catalogues, the volume of the catalogues to be printed, the decision as to whom to mail the catalogues, and the frequency of the mailings.

The catalogue provided promotion or advertising for the local store. The last page of most of the catalogues stated "Please Visit Our Stores" and then listed the name and address of the three stores, including the New York store. While the catalogue revealed the location of each of HSC's retail stores, the purpose of the reference, in terms of the preparer's job responsibility, was to promote the catalogue, not the retail stores. It is petitioner's belief that the reference to the stores promotes the catalogue by showing that petitioner is a real company.

HSC has been informed by many of its subscribers that they subscribed to the catalogue solely for its informational value. They also informed petitioner that they subscribe to the catalogue to be better informed as the best and/or most innovative products commercially available.

HSC catalogue articles were detailed and gave as much information about the product as possible because subscribers liked to read the catalogue's content.

HSC selected its products and made business decisions as to what products to include in the catalogue based upon the criteria that the products were rated the best or the only one of a particular product category, or represent a product innovation in a particular product category. The catalogue advised its subscribers of products that had been rated the best or the only one of a product in a particular category. The articles on products in HSC's catalogue were written by different authors.

The Institute regularly conducted tests to help customers make easier buying decisions. The products were tested in side-by-side comparisons under actual conditions of use. Whenever possible, the Institute's personnel conducted these tests with the help of customer panelists, who examined factors such as performance, design and ease of use. Through testing by the Institute, HSC has been able to offer the easiest-to-operate VCR, the best digital answering machine, and the best electronic blood pressure monitor. HSC's catalogue offered such unique products as "[t]he only self-righting walking cane," which, after testing, was rated a grand prize winner by the Institute and also was featured in the Journal of the American Medical Association; the advanced interactive flight simulator pod; the Bose wave radio (which received the Best of What's New Award by Popular Science); and the feline drinking fountain, which was recommended by veterinarians.

The Institute's analysis and test results regarding products were not sold or shared with anyone other than HSC. Accordingly, the Institute's analysis of strength, quality, innovativeness and uniqueness of products was not available to consumers except through the HSC catalogue.

In 1991, HSC's catalogue contained advertisements for Dodge car products under the headline "Innovation Defined." HSC was paid by Dodge to advertise its car products in the HSC catalogue. HSC did not sell Dodge car products through its catalogue or otherwise. It was rare for petitioner to accept advertising from other customers.

The catalogue was devoted to the field of innovation. HSC's products have been displayed at Walt Disney World's Epcot Center, featured as "Innoventional."

Retail Stores

HSC had retail stores located in Chicago, Illinois, New York, New York and Beverly Hills, California. As noted, HSC employed approximately 70 people in Chicago. Petitioner employed approximately 20 to 25 people in New York and approximately 10 people in California.

The retail operations and the catalogue operations were run by HSC like separate companies. They were viewed by HSC as entirely separate businesses with different objectives. The retail operations and the catalogue operations had separate books and records, including separate profit and loss statements. Approximately 10 to 15 percent of the total sales occurred through the retail stores. At some juncture, the company produced one profit and loss statement for the entire company although the retail segment was always broken out so that it could be evaluated separately.

The retail stores obtained some of their merchandise directly from vendors. However, most of the merchandise came from the Ohio warehouse. Generally, the products advertised for sale in the catalogue were also offered for sale in the store.

Occasionally, if the retail store did not have a particular item in stock, it would place an order for the customer in the catalogue. In the later years, the store had a method of accessing the catalogue system on behalf of the customer.

Although it was not something that petitioner encouraged, customers who purchased merchandise through the catalogue could return products to the store in New York. HSC offered an unconditional guarantee through its catalogue which included postage and handling. So if a customer wanted to return the product obtained through the catalogue it would be at no cost. It was also usually simpler because it could be picked up and shipped through UPS to the warehouse where it would ultimately end up.

The performance of the HSC employees responsible for the retail operations was not evaluated or in any way based upon the success or failure of the catalogue operations. The performance of the HSC employees responsible for the catalogue operations was not evaluated or in any way based upon the success or failure of the retail operations.

During the period in issue, information related to the retail operations was maintained on a point of sale computer system separate from the mainframe used for the catalogue operations. Each retail store had its own computer for the transaction of business, on which was maintained inventory information and sales transactions unique to that retail store. The computers for the retail stores did not maintain any financial or expense information relating to the catalogue operations.

During the audit period, information for the catalogue operations was maintained on a mainframe computer located in Ohio, on which was stored inventory data for the catalogue operations, catalogue order information, as well as financial data for the catalogue operation.

The computer systems for the retail business had no ability to communicate with the computer system for the catalogue business, and vice versa.

Inventory information from the retail store's computer was transferred to Chicago so that inventory control personnel could monitor the store's inventory level. The same management personnel who performed financial and treasury functions in Chicago on behalf of the catalogue operations also performed financial and treasury functions on behalf of the retail stores. Further, the same accounts payable staff who paid the bills for the catalogue operations paid the bills for the retail stores. At the senior management level, corporate staff oversaw both functions.

HSC's New York employees did not have any responsibility or authority for the printing or distribution of the catalogue. HSC did not engage in any activities within New York with regard to the distribution of the catalogue. It did not exercise any control over the catalogues within New York State.

The presence of HSC's retail store in New York did not have any effect on HSC's distribution of catalogues in New York.

HSC employees involved in preparing the catalogue did not have any responsibility for promoting sales in the New York retail store.

Had HSC known that the State of New York would seek to impose sales or use tax on HSC catalogues shipped into New York, HSC would have set up separate legal entities for its retail business and catalogue business.

HSC's corporate accounting department charged the New York store for catalogues which were available for distribution out of the New York retail store during the audit period. There were no telephones or computer terminals dedicated for customer use in placing catalogue orders.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

In his determination, the Administrative Law Judge noted that Article 28 of the Tax Law provides for the imposition of sales and use tax on the retail sale of tangible personal property and on the providing of certain enumerated services. Tax Law § 1110(a) imposes a compensating use tax on the use within New York of any tangible personal property upon which the service of printing has been performed. The tax is based upon the consideration given or contracted to be given for the service. The Administrative Law Judge further noted that Tax Law § 1115(a)(5) exempts all receipts from the sale of newspapers and periodicals from sales and use tax. In analyzing relevant regulations interpreting Tax Law § 1115(a)(5), the Administrative Law Judge found that petitioner would have to demonstrate that its catalogues qualified as “periodicals” in order to avail itself of the exemption provided by that section. Although the term “periodical” was not defined in Tax Law § 1115(a)(5), the Division’s regulations at 20 NYCRR 528.6(c)(1) provided five criteria which must be present in order to find that a publication was a periodical.

The Administrative Law Judge concluded that petitioner’s publications met all the requirements of a periodical except for the fifth criteria; i.e., that each issue of the publication must contain a variety of “articles by different authors devoted to literature, the sciences, or the arts, news, some special industry, profession, sport or other field of endeavor” (20 NYCRR 528.6[c][1]). Relying on a dictionary definition of the term “article,” the Administrative Law Judge found that petitioner’s catalogues contained articles because the product descriptions contained in the catalogues constituted short nonfictional prose, they formed an independent portion of the publication and they were apparently written by different authors. However, the

Administrative Law Judge concluded that the articles contained in each issue were not devoted to literature, the sciences, or the arts, news, some special industry, profession, sport or other field of endeavor as required by the regulations. Rather, they were devoted to selling the products in the catalogue and consequently did not satisfy the fifth criteria of the regulatory definition of a periodical. Additionally, the Administrative Law Judge noted that this conclusion was compelled by 20 NYCRR 528.6(c)(3) which provided that advertising material, such as catalogues, shall not be exempt as a periodical.

The Administrative Law Judge considered petitioner's argument that the Division's regulations required the type of content-based analysis prohibited by the First Amendment. Relying on *Regan v. Taxation with Representation* (461 US 540, 76 L Ed 2d 129), *Leathers v. Medlock* (499 US 439, 113 L Ed 2d 494, *cert denied* 508 US 960, 124 L Ed 2d 680) and *Stahlbrodt v. Commissioner of Taxation & Fin.* (92 NY2d 646, 684 NYS2d 466), the Administrative Law Judge concluded that petitioner's First Amendment objections were without merit. First, the Administrative Law Judge found it clear that the sales and use tax is a tax of general application and is not directed at particular publications. Other forms of published commercial speech which are distributed without charge do not benefit from an exemption from sales tax for the purchase of printing services. Second, the Administrative Law Judge found that the Legislature intended to restrict the benefits of the exemption to particular publications and exclude those publications of purely commercial interest. The exemption at issue in this matter does not enforce differential treatment on the basis of ideas or viewpoints set forth in petitioner's catalogue. The Administrative Law Judge concluded that here, unlike the situation present in *Arkansas Writers' Project v. Ragland* (481 US 221, 95 L Ed 2d 209), the tax burden does not

fall on a small group of publications. Rather, the tax in issue is also imposed on, among other things, other catalogues, advertising fliers, travel brochures, telephone directories, shipping and restaurant guides, and shopping center advertising sheets (*cf.*, Tax Law § 1115[i][D]). Nor, concluded the Administrative Law Judge, is this a case where a publication is being penalized for the particular coverage it provides. Rather, the Legislature has decided not to subsidize a particular type of publication which does not serve the same social purpose by informing the public of matters of community interest rather than matters of purely commercial interest. The Administrative Law Judge concluded that the Division's determination that petitioner's catalogues are not periodicals was not based on the content or viewpoint of any material found in petitioner's publication but because petitioner's publication satisfies the definition of what is commonly understood to be a catalogue.

The Administrative Law Judge disagreed with the Division's position that petitioner was raising a challenge to the facial validity of Tax Law § 1115(a)(5) and, therefore, it was beyond the jurisdiction of the Division of Tax Appeals to consider such argument. The Administrative Law Judge noted that the Legislature has given the Tax Appeals Tribunal authority to rule on the validity of the Division's regulations where they are at issue and it follows that the Division of Tax Appeals has the authority to determine whether a regulation is a proper interpretation of a statute. The Administrative Law Judge concluded that petitioner's objection was to the Division's regulation, not the statute, and there was no barrier to a consideration of petitioner's constitutional argument.

The Administrative Law Judge rejected petitioner's assertion that the assessment of use tax for literature sent to New York residents violates the Commerce Clause of the United States

Constitution and the New York State Constitution because petitioner is not involved in the printing or distribution of the catalogues and engages in no printing or distribution within New York. The Administrative Law Judge found that petitioner's argument runs contrary to the statutory scheme of a "use" provided in Tax Law § 1101(b)(7) which encompasses the distribution of advertising catalogues. The "use," i.e., the distribution of the catalogues, occurred within New York when those catalogues were received by petitioner's customers in New York. The Administrative Law Judge found that although the Postal Service carried out the actual delivery of the catalogues, petitioner exercised complete power and control over them. The Administrative Law Judge concluded that, based on the record, petitioner has far more than the slightest presence in New York, as required to meet the standards required by the Commerce Clause for sufficient nexus to support the imposition of use tax on catalogues which were printed outside of New York and shipped to prospective customers within the State.

Further, the Administrative Law Judge refused to accept petitioner's argument that the New York City portion of the tax must be abated because New York City did not amend its definition of "use" to include the distribution of property. The Administrative Law Judge concluded that petitioner's argument did not take into account the provisions of Tax Law § 1107(a) which mandate that the definition of use for a tax imposed within New York City be the same as that used by New York State.

Finally, the Administrative Law Judge denied petitioner's claim that it was entitled to a refund of 44 percent of the tax paid for the first audit period and 41 percent for the second audit period because these percentages constituted the cost of printing the catalogues in Tennessee.

Petitioner argued that the statute does not apply to printing and any application of the tax laws to out-of-state printing violates the Commerce Clause.

The Administrative Law Judge determined that this case involves the right of New York to tax the distribution of property within New York. Relying on the provisions of Tax Law § 1110, the Administrative Law Judge upheld the right of the Division to impose a use tax on the cost of the printing service.

ARGUMENTS ON EXCEPTION

On exception, petitioner asserts the identical arguments that it presented to the Administrative Law Judge. It argues that it is a violation of the First Amendment of the United States Constitution to impose a use tax on its catalogues while not imposing the same tax on periodicals. Petitioner claims that its catalogues are periodicals that contain articles on the subject of innovation in consumer products. By taxing its publication on the grounds that it is a catalogue while not taxing other periodicals, petitioner asserts that New York is making content-based distinctions between commercial speech and noncommercial speech in violation of the First Amendment. Petitioner also posits that the assessment violates the Commerce Clause of the United States Constitution because there is no substantial nexus between the activity of mailing a catalogue and the State of New York. Petitioner further urges that the mailing of the catalogue into New York from outside of the State does not constitute a “use” within the State. In the alternative, petitioner maintains that the portion of the tax based on distribution of catalogues in New York City and the portion of the tax that is based on the costs of printing should be refunded.

The Division, in response, argues that the Administrative Law Judge's conclusion is correct except for one issue. As to that issue, the Division claims in support of its own exception that the Administrative Law Judge incorrectly considered whether petitioner's catalogues were periodicals. The Division posits that once the Administrative Law Judge concluded that these publications were catalogues, they could not, pursuant to the Division's regulations, ever be considered periodicals. Thus, there was no basis for the Administrative Law Judge to even consider whether the individual product descriptions qualified as "articles," as that term is commonly defined.

OPINION

Pursuant to Tax Law § 1105, New York imposes a sales tax on receipts from the retail sale of tangible personal property and certain enumerated services. In addition, Tax Law § 1110(a) imposes a use tax on the use within New York of tangible personal property upon which the service of printing has been performed. "Use" is defined by Tax Law § 1101(b)(7) as:

[t]he exercise of any right or power over tangible personal property by the purchaser thereof and includes, but is not limited to, the receiving, storage or any keeping or retention for any length of time, withdrawal from storage, any installation, any affixation to real or personal property, or any consumption of such property. Without limiting the foregoing, use also shall include the distribution of only tangible personal property, such as promotional materials (emphasis added).

In this instance, use tax was imposed on petitioner for its distribution of catalogues in New York. The tax was based upon the consideration given or contracted to be given for the service of printing these catalogues. Approximately 40 percent of the use tax assessments was

based on the cost of printing and approximately 60 percent of the use tax assessments was based on the cost of the paper used to produce these catalogues.

At issue in this proceeding is whether New York may impose use tax on petitioner's printing costs in the first instance and, if so, whether petitioner is entitled to claim the benefit of the exemption from sales tax and the compensating use tax on receipts from the sale of newspapers and periodicals provided by Tax Law § 1115(a)(5).

We first note that there is no definition of a "periodical" in Article 28 of the Tax Law. However, sales tax regulations issued by the Division define the word "periodical" as used in section 1115(a)(5) as follows:

In order to constitute a periodical, a publication must conform generally to the following requirements:

(i) it must be published in printed or written form at stated intervals, at least as frequently as four times a year;

(ii) it must not, either singly or, when successive issues are put together, constitute a book;

(iii) it must be available for circulation to the public;

(iv) it must have continuity as to title and general nature of content from issue to issue; and

(v) each issue must contain a variety of *articles by different authors devoted to literature, the sciences, or the arts, news, some special industry, profession, sport or other field of endeavor* (20 NYCRR 528.6[c][1]; emphasis added).

Section 528.6(c)(3) of the Division's regulations provides that: "[n]othing in this section shall be construed to exempt as a periodical the following: . . . advertising material, such as catalogs, flyers, pamphlets and brochures."

The Administrative Law Judge considered whether or not petitioner's catalogues distributed in New York met the regulatory definition of a "periodical." After analyzing each of the five requirements which the Division's regulations prescribe in order for a publication to be considered a periodical, the Administrative Law Judge concluded that petitioner's catalogues met the first four requirements. As to the fifth and final requirement, the Administrative Law Judge concluded that the catalogues contained a variety of articles by different authors but that these articles were not devoted to "literature, the sciences, or the arts, news, some special industry, profession, sport or other field of endeavor" as required. Absent that, the Administrative Law Judge concluded that petitioner was not eligible for the exemption provided by Tax Law § 1115(a)(5).

The Division has taken exception to the Administrative Law Judge's findings that petitioner's catalogues contained "articles" by different authors. The Division argues that petitioner's catalogues could not be exempt from sales tax as periodicals because they are advertising material pursuant to 20 NYCRR 528.6(c)(3)(i). As a result, the Division asserts that the Administrative Law Judge incorrectly considered whether despite their status as advertising material, they could also be periodicals. We disagree with this position.

First, Tax Law § 1115(a)(5) does not contain any mention of "advertising material" or indicate in any respect that in determining what constitutes a newspaper or periodical entitled to exemption from sales and use tax, the presence of "advertising material" has any significance. Nor has the Division explained in its regulations exactly what "advertising material" is or when a publication may or may not be considered to be "advertising material." Relying on *Matter of Scotsmen Press v. Tax Appeals Tribunal* (165 AD2d 630, 569 NYS2d 991), the Division argues

that petitioner's catalogues are clearly advertisements in that they contain public announcements concerning things for sale. In *Scotsmen*, the issue before the Court was whether it was rational for the Division to consider certain items as "advertising" in determining whether the advertisements in petitioner's publication exceeded 90 percent of the printed area of all issues of the publication averaged on an annual basis. This, in turn, determined whether or not petitioner's publications were exempt as "shopping papers" pursuant to Tax Law § 1115(i)(C). That, however, is not the issue before us. The issue to be decided herein is whether petitioner's publications are periodicals entitled to exemption pursuant to Tax Law § 1115(a)(5). Contrary to the Division's position, that statute does not provide that a periodical may not contain advertising material. Assuming that a periodical may contain advertising material, the Division points to no authority which explains at what point, if any, an otherwise qualifying periodical may become a non-periodical due to the quantity of advertising material contained within its covers. Therefore, we agree that the Administrative Law Judge proceeded correctly in his analysis of petitioner's publications and deny the exception of the Division.

Shortly after the Administrative Law Judge issued his determination in this proceeding, we issued our decision in *Matter of Sharper Image Corp.* (Tax Appeals Tribunal, November 24, 1999). The facts in *Sharper Image* are remarkably similar to those presented herein. In both cases, petitioners were out-of-state corporations which sold merchandise by mail order and at retail locations throughout the United States, including at least one store in New York City. Each petitioner produced a catalogue several times a year. The ultimate purpose of the catalogues was to have customers purchase the products advertised. All decisions regarding these catalogues were made outside New York, including selecting the content of the catalogues, the volume of

the catalogues to be printed, the recipients of the catalogues, and the frequency of the mailings. The catalogues distributed by each petitioner were prepared entirely out of state, as well as printed out of state. No activities related to the design, printing or distribution of the catalogues were performed in New York. No New York personnel were involved in either the preparation of the text or product photographs for the catalogue. Catalogues contained little prose except product descriptions.

The issues raised and decided in *Sharper Image* are among those raised for consideration herein and are conclusive on such issues. In *Sharper Image*, applying the principles and analysis espoused in *Stahlbrodt v. Commissioner of Taxation & Fin.* (*supra*), we concluded that the Division's regulation defining a "periodical" for purposes of Tax Law § 1115(a) does not violate the First Amendment because that regulation did not attempt to selectively tax a targeted group nor was it content-based. Additionally, we found unpersuasive petitioner's argument that the amendment to Tax Law § 1101(b)(7) resulting from the decision in *Matter of Bennett Bros. v. State Tax Commn.* (62 AD2d 614, 405 NYS2d 803) which expanded the definition of the term "use" to include the distribution of promotional materials did not apply to it because it was an out-of-state corporation. As a New York vendor, the amendment to Tax Law § 1101(b)(7) certainly applied to petitioner. Petitioner made use of its catalogues by directing the distribution of such catalogues to addressees in New York as well as to its retail stores in New York. Thus, we found the petitioner in *Sharper Image* properly liable for the use tax. So, too, we find the same arguments raised by petitioner herein unavailing. The analysis by the Administrative Law Judge in the instant proceeding is consistent in all respects with our decision in *Sharper Image* and we agree with the conclusion of the Administrative Law Judge that petitioner's catalogues do

not constitute periodicals and are not entitled to the exemption from taxation provided by Tax Law § 1115(a). We also find that the Administrative Law Judge was correct in his conclusion that the Division's regulation does not violate the First Amendment of the Constitution by making a content-based distinction between commercial speech and noncommercial speech.

As to the remaining arguments made by petitioner in the instant case, we find that petitioner has failed to demonstrate that the Administrative Law Judge's conclusions are incorrect. Although New York City has not amended its definition of "use" to make it consistent with the definition provided in Tax Law § 1101(b)(7) (*see*, Administrative Code of City of NY § 11-2001[7]), Tax Law § 1107(a) requires that the definition of "use" for a tax imposed within New York City must be the same as that used by New York State. Thus, there is no basis for refunding that portion of the use tax allocable to New York City.

Petitioner argues that in order to sustain a direct tax on a company that engages in interstate transactions, such as the mailing of promotional materials from outside the state to New York residents, the Division must establish that there is a relationship between the activity to be taxed (and not just to petitioner itself) and the seller's activity within New York. We believe that such a relationship is demonstrated based on the facts of this case. Here, we adopt the conclusions of the Administrative Law Judge on this issue:

Clearly, the record establishes that petitioner has far more than the slightest presence in New York. As noted by the Division, petitioner operated a retail store in New York. In addition, the catalogues provided advertising for the New York retail store. The retail stores, in turn, assisted the catalogue sales by accepting returns of merchandise from catalogue customers, by accepting names and addresses of customers for the catalogue mailing list, by distributing registration cards, by automatically entering names of store customers that request delivery in a mail order database and

by placing catalogue orders for store customers when a product is unavailable at the store. Clearly, these contacts satisfy the standards established in *National Geographic Socy. v. California Bd. of Equalization* (430 US 551, 51 L Ed 2d 631) and *Matter of Orvis Co. v. Tax Appeals Tribunal* (86 NY2d 165, 630 NYS2d 680, *cert denied* 516 US 989, 133 L Ed 2d 426). Further support for this position may be found in *D. H. Holmes Co. v. McNamara* (486 US 24, 100 L Ed 21) where, on a similar set of facts, the Supreme Court applied the standards employed in *National Geographic* and concluded that there was a sufficient nexus to support the imposition of use tax on catalogues which were printed outside of Louisiana and shipped to prospective customers within the State (Determination, conclusion of law “P”).

After carefully reviewing the record in this matter, we find that the Administrative Law Judge has fully and correctly addressed each of the issues raised by petitioner herein. On exception, neither petitioner nor the Division has presented any basis for modifying the Administrative Law Judge’s determination in any respect. As a result, we deny both petitioner’s and the Division’s exceptions and affirm the determination of the Administrative Law Judge in this matter.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Hammacher Schlemmer Co., Inc. is denied;
2. The exception of the Division of Taxation is denied;
3. The determination of the Administrative Law Judge is affirmed;
4. The petitions of Hammacher Schlemmer Co., Inc. are denied; and

5. The denials of the refund claims are sustained.

DATED: Troy, New York
November 22, 2000

/s/Donald C. DeWitt

Donald C. DeWitt
President

/s/Carroll R. Jenkins

Carroll R. Jenkins
Commissioner

/s/Joseph W. Pinto, Jr.

Joseph W. Pinto, Jr.
Commissioner