

New York State Department of Taxation and Finance
Office of Counsel
Advisory Opinion Unit

TSB-A-10(8)C
Corporation Tax
June 25, 2010

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C090827A

The Department received a petition from [REDACTED] (“Petitioner”) relating to the New York corporate franchise tax. Petitioner asks whether sales of products and services to customers within New York State would subject it to New York State corporate taxes. If it is subject to tax in New York, Petitioner asks whether the tax is based on all the New York receipts, or just the portion of the receipts attributable to those activities that subjected the corporation to taxation in New York State.

We conclude that if Petitioner sells and ships its products from [REDACTED] State to a customer in New York State, it will not be subject to the Article 9-A corporate franchise tax if its activities in New York State fall within the exception created by Public Law 86-272. If Petitioner’s only activity in the state is solicitation of orders for tangible personal property, it will meet this standard and therefore not be subject to New York corporate franchise tax.

If, in addition to selling and shipping its products to New York customers, Petitioner also sends its employees or agents to New York to perform installation, training, and repairs, it will no longer qualify for the exemption under Public Law 86-272. Therefore, Petitioner will be subject to Article 9-A corporate franchise tax.

If Petitioner is required to pay New York Article 9-A corporate franchise tax, the tax will be calculated according to the apportionment method described in the statute.

Facts

Petitioner is a [REDACTED] corporation that sells testing equipment used by R&D departments of corporations, governments, and universities. It does not currently do any business within New York State. Petitioner bills its customers separately for sales of equipment, installation, and training. Generally, the amount Petitioner bills its customers for installation and training services makes up about 1-2% of its total invoices for testing systems.

While Petitioner does not currently do any business within New York State, the corporation has a potential customer in New York and would like to determine its exposure to tax liability if the customer chooses to purchase Petitioner’s testing systems.

Analysis

A. Will Petitioner be subject to Article 9-A corporate franchise tax if its activity in the state is limited to selling equipment to New York customers?

Every foreign corporation that does business, employs capital, owns or leases property in a corporate or organized capacity, or maintains an office in New York State (whether or not the corporation has been authorized by the Department of State) is subject to tax under Article 9-A of the Tax Law and

must file a corporate tax return and pay the franchise tax imposed by that article. Tax Law § 209(1); *see* NEW YORK STATE DEPARTMENT OF TAXATION AND FINANCE PUBLICATION 20: TAX GUIDE FOR NEW BUSINESSES (“Pub-20”) (October 2007) 8-9.

Each corporation subject to tax under Article 9-A of the Tax Law computes a tax on four different measures: a tax measured by the entire net income base, a tax measured by the capital base, a tax measured by the minimum taxable income base, and a tax measured by the fixed dollar minimum. The corporation pays the highest computed tax, plus a tax on the subsidiary capital base, if applicable. Tax Law § 210.1; *see* Pub-20 at 10.

However, an exception exists under Public Law 86-272, as described in Section 1-3.2(a)(3) of the Article 9-A Regulations. Foreign corporations are exempt from corporate franchise tax if their employees’ and representatives’ activity is “. . . limited to the solicitation of orders. The solicitation of orders includes offering tangible personal property for sale or pursuing offers for the purchase of tangible personal property and those ancillary activities, other than maintaining an office, that serve no independent business function apart from their connection to the solicitation of orders.” 20 NYCRR 1-3.4(b)(9)(iv). Approval or rejection of the orders must take place outside the state. 20 NYCRR 1-3.4(b)(9)(i).

In order to meet these criteria for exemption, Petitioner must satisfy three separate conditions. First, the testing systems sold by Petitioner to New York customers must consist solely of tangible personal property. Second, Petitioner must restrict its activity in New York to the solicitation of orders. Finally, the orders Petitioner solicits in New York must be approved or rejected outside of New York State. If Petitioner’s sale of testing equipment to its customer in New York meets these conditions, Petitioner will not be subject to corporate franchise tax under Article 9-A.

B. Will Petitioner be subject to Article 9-A corporate franchise tax if, in addition to selling equipment to New York customers, it also provides installation and training services to its New York customers that have purchased this equipment?

If its activities in New York State go beyond the solicitation of orders, a corporation will be subject to tax in New York State unless such activities are de minimis. 20 NYCRR 1-3.4(b)(9)(v). “Activities will not be considered de minimis if such activities establish a nontrivial additional connection with New York State. . . . Examples of activities which go beyond the solicitation of orders include: (a) making repairs to or installing the corporation’s products. . . [and] (f) giving technical advice on the use of the corporation’s products after the products have been delivered to the customer.” *Id.*

The activities contemplated by Petitioner, namely, installation, training, and service calls, clearly fall within those that would subject a foreign corporation to tax. Therefore, if Petitioner sends its employees or agents to New York to provide installation and training for the testing systems it has sold after the systems have been delivered to a customer, or if it sends its employees or agents to New York to perform service calls on equipment, the corporation will be subject to Article 9-A corporate franchise tax.

C. If Petitioner is subject to Article 9-A corporate franchise tax, how will its tax liability be calculated?

A corporation subject to tax under Article 9-A must calculate its tax under each of four bases set forth in Tax Law § 210, and is liable for the highest amount. 20 NYCRR 3-1.2.

The entire net income base is the portion of the taxpayer's entire net income that is allocated to New York. 20 NYCRR 3-2.1(a). A taxpayer's entire net income is divided into business income and investment income. 20 NYCRR 3-2.1(b). Business income is allocated to New York by a business allocation percentage ("BAP"). *Id.* The business allocation percentage is a fraction, the numerator of which is the taxpayer's business receipts within New York for the reporting period, and the denominator of which is the taxpayer's business receipts within and without New York for the reporting period. Tax Law § 210.3(a)(10); 20 NYCRR 4-4.1(a). Investment income is allocated to New York by an investment allocation percentage. Tax Law § 210.3(b).

The minimum taxable income base, another of the four bases within Tax Law § 210, uses the taxpayer's entire net income as a starting point. Tax Law § 208.8-B (a). The final base, the fixed dollar minimum, is only used when the amount calculated under the other three bases is less than \$5,000. Tax Law § 210.1(d). The fixed dollar minimum varies based on the taxpayer's total gross payroll. *Id.*

It appears from the facts presented, and we will assume for the purposes of this advisory opinion, that Petitioner has no capital assets in New York and no subsidiaries. Based on this assumption, the remaining two bases – the capital base and the subsidiary capital base – would not be applicable to Petitioner. We will also assume that the taxpayer's tax based on entire net income exceeds \$5,000, and therefore the fixed dollar minimum is also inapplicable. Because the minimum taxable income base and the entire net income base are both determined by calculating the taxpayer's entire net income as a starting point, the following discussion of how the taxpayer's activities in New York affect its tax liability is relevant regardless of whether the taxpayer must ultimately pay on the minimum taxable income base or the entire net income base.

When calculating the BAP that is used to determine entire net income, the taxpayer must include all receipts from sales of tangible personal property shipped to New York State, all receipts from services performed in New York State, and all other business receipts "earned" in New York State within the numerator. 20 NYCRR 4-4.1. Public Law 86-272 does not provide for any partial exemption for those activities that would be exempt if they were the only activities the taxpayer engaged in within the state. 20 NYCRR 1-3.4(b)(9)(iv)-(v). If a taxpayer is not exempt from taxation under Public Law 86-272, it is subject to tax on all its activities. *See* 20 NYCRR 1-3.2(a)(2); *also see* 20 NYCRR 1-3.2(f)(5)-(6). Its liability to New York State is based on its business allocation percentage, a fraction that uses the taxpayer's total receipts within and without the state as its denominator.

Therefore, the correct answer to petitioner's question as to whether its corporation tax liability would be "only on the installation, training, or service portion of the invoice" or "for the total invoiced to customers in New York State" is neither. New York State does not use a separate accounting system, which "involves identifying all items of income and costs that are related to the taxpayer's activities within the taxing state and constructing a statewide net income from these items." 1 HELLERSTEIN & HELLERSTEIN 3d ¶ 8.03 (3d ed. 2000).

As a result, Petitioner's corporate franchise tax liability will not be based solely on its invoices to New York customers. By multiplying its total business income by its BAP, Petitioner will arrive at the amount of business income that is attributed to New York. Total entire net income attributable to New York is the sum of a taxpayer's allocated business income and its allocated investment income.

In conclusion, Petitioner will be subject to Article 9-A corporate franchise tax if its activities in New York State exceed the exemption for the exclusive solicitation of orders provided for in Public Law 86-272. If Petitioner is subject to the corporate franchise tax, all of Petitioner's business receipts

allocated to New York will be included in the numerator of its business allocation percentage, and used to calculate the share of its entire net income that is apportioned to New York to calculate the corporation's tax liability.

DATED: June 25, 2010

/S/

Jonathan Pessen
Director of Advisory Opinions
Office of Counsel

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