New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-91(18)C
Corporation Tax
September 23, 1991

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO.C910606A

On June 6, 1991, a Petition for Advisory Opinion was received from Anonymous, c/o Robert L. Kohl, Esq., Gaston & Snow, 666 Fifth Avenue, New York, New York 10103.

The issue raised by Petitioner is whether a Delaware corporation whose sole place of business is in Texas is subject to tax under Article 9-A of the Tax Law when it is engaged in the business of trading stocks, bonds, options and other financial instruments on various stock exchanges located in New York and elsewhere, and acts as a "specialist" or "market maker" with respect to certain options that are traded on the American Stock Exchange.

A Delaware corporation (hereinafter "Taxpayer") has elected to be taxed as an S corporation for federal income tax purposes. Taxpayer's sole shareholder is a resident of the state of Texas. Taxpayer's sole place of business is located in Houston, Texas. Taxpayer does not maintain an office anywhere other than within Texas, but does have its "registered representative" (an employee performing certain regulated services) located in Chicago, Illinois. Certain of Taxpayer's directors are located in New York State. Taxpayer is a registered broker-dealer under the Securities and Exchange Act of 1934.

Taxpayer is engaged in the business of trading stocks, bonds, options and other financial instruments on the various stock exchanges located in New York and elsewhere. Taxpayer's activities within New York State consist of the buying and selling of stocks and securities on stock exchanges for its own account and on behalf of a limited number of clients, for which it is paid a commission. Taxpayer's securities transactions, both for its own account and client transactions, are executed through independent brokers.

In addition to the proprietary and commission trades described above, Taxpayer acts as a "specialist" or "market maker" with respect to certain options that are traded on the American Stock Exchange (hereinafter "AMEX"). The Taxpayer's role as a specialist requires it to maintain a fair and orderly market in such securities and to ensure that there will always be (and sometimes act as) a ready buyer or seller for the AMEX-traded options. As a specialist, in order to maintain the market, Taxpayer buys and sells certain AMEX-traded options for its own account. Unlike many specialists, all of Taxpayer's trades as a specialist are executed through independent brokers.

The AMEX rules require Taxpayer to be a "member corporation" of the AMEX to act as a specialist for the AMEX-traded options. To be a member corporation, the rules require that the corporation be associated with at least one regular or options "principal member" of the AMEX. The AMEX rules further provide that a principal member acting as a specialist must initiate and effect

transactions on the AMEX without interference with or control over such transactions by the member corporation. In order to comply with these rules, Taxpayer has entered into an agreement (hereinafter "Agreement") with an individual (hereinafter "X"), an AMEX principal member, whereby X will qualify Taxpayer as an AMEX member corporation.

Under the Agreement, Taxpayer and X have agreed to create a market maker operation, i.e., act as a specialist, with respect to the AMEX-traded options. Under the Agreement, X maintains a seat on the AMEX, which X leases from an unrelated third party pursuant to a Model Special Transfer Agreement (hereinafter "Seat Lease"). Pursuant to the terms of the Agreement, Taxpayer pays a fee to X for acting as Taxpayer's principal member by making all Seat Lease rental payments (of $1,000 per month), and paying all floor expenses incurred in connection with the use of the seat, including AMEX membership fees, dues, and telephone fees. X has the right to use the seat for his own benefit for no consideration. All commissions and other profits from trades by X remain the sole and exclusive property of X.

X, and not Taxpayer, is the lessee under the terms of the Seat Lease; the Seat Lease denominates X as Taxpayer's "employee," but recognizes that X is qualifying Taxpayer as a member organization. The Seat Lease terminates if X can no longer qualify Taxpayer as a member of the AMEX. In this event, in order to continue to qualify as an AMEX specialist, Taxpayer must nominate another "employee" as lessee who must enter into a new lease with the lessor. If X ceases to use the seat or the Agreement is terminated, Taxpayer is still responsible for the payments due to the lessor under the Seat Lease.

A seat on the AMEX provides the holder with the "privilege of conducting the business of the buying and selling of securities on the floor of the exchange." All of Taxpayer's trades are executed through independent brokers. From the Taxpayer's perspective, the AMEX imposed requirement that it maintain a seat is the equivalent of a license to do business in the securities industry.

Taxpayer will occasionally execute trades with X, for which X is paid an arm's length fee, commensurate with the fees that X charges other persons. X is required to use his own judgment, experience and expertise in executing transactions on the AMEX. Taxpayer does not pay any salary or other compensation to X, other than pursuant to the Agreement and the arm's length commissions for occasional trades.

Section 209.1 of Article 9-A of the Tax Law imposes the business corporation franchise tax on every foreign corporation, unless specifically exempt, for the privilege of doing business, or of employing capital, or of owning or leasing property in New York State in a corporate or organized capacity, or of maintaining an office in New York State.

Section 1-3.2(b) of the Business Corporation Franchise Tax Regulations (hereinafter "Article 9-A Regulations") provides that:

(1) [t]he term doing business is used in a comprehensive sense and includes all activities which occupy the time or labor of men for profit. Regardless of the nature of its activities, every corporation organized for profit and carrying out any of the purposes of its organization is deemed to be doing business for the purposes of the tax. In determining whether a corporation is doing business, it is immaterial whether its activities actually result in a profit or a loss.

(2) Whether a corporation is doing business in New York State is determined by the facts in each case. Consideration is given to such factors as:

(i) the nature, continuity, frequency, and regularity of the activities of the corporation in New York State, compared with the nature, continuity, frequency, and regularity of its activities elsewhere;

(ii) the purposes for which the corporation was organized, compared with its activities in New York State;

(iii) the location of its offices and other places of business;

(iv) the income of the corporation and the portion thereof derived from activities in New York State;

(v) the employment in New York State of agents, officers and employees; and

(vi) the location of the actual seat of management or control of the corporation.

Section 1-3.2(c) of the Article 9-A Regulations provides that:

[t]he term employing capital is used in a comprehensive sense. Any of a large variety of uses, which may overlap other activities, may give rise to taxable status. In general, the use of assets in maintaining or aiding the corporate enterprise or activity in New York State will make the corporation subject to tax. Employing capital includes such activities as:

(1) maintaining stockpiles of raw materials or inventories; or

(2) owning materials and equipment assembled for construction.

Section 1-3.2(d) of the Article 9-A Regulations provides that:

[t]he owning or leasing of real or personal property within New York State constitutes an activity which subjects a foreign corporation to tax. Property owned by or held for the taxpayer in New York State, whether or not used in the taxpayer's business, is sufficient to make the corporation subject to tax.

Property held, stored or warehoused in New York State creates taxable status. Property held as a nominee for the benefit of others creates taxable status ....

Section 1-3.2(e) of the Article 9-A Regulations provides that:

> [a] foreign corporation which maintains an office in New York State is engaged in an activity which makes it subject to tax. An office is any area, enclosure or facility which is used in the regular course of the corporate business. A salesman's home, a hotel room, or a trailer used on a construction job site may constitute an office.

In Cargill Financial Services Corporation, Adv Op Comm T&F, September 26, 1990, TSB-A-90(20)C, a foreign corporation was engaged in the business of trading in stocks, bonds, currencies, commodities and other financial instruments on various exchanges in New York City whereby the transactions were executed by independent brokers. The Commissioner advised that such activity by itself was notsufficient to deem Cargill to be doing business in New York State. Herein, Taxpayer's activities involve more than merely trading securities through an independent broker. Taxpayer and X have an agreement that states "The parties hereto agree to form a 'market maker' operation, to their mutual benefit during the period January 11, 1991 to January 11, 1992." Under the agreement X leases a seat on the AMEX for which Taxpayer will pay all the expenses including Seat Lease rental payments, AMEX membership fees, dues and telephone fees. X will ensure that Taxpayer qualifies as a specialist.

Specialists are members of the AMEX whose obligation is to maintain a fair and orderly market in the options in which they are registered. Towards that end, they perform three functions. First, specialists act as brokers' brokers, holding away-from-the market orders entrusted to them by brokers on behalf of customers. These limit orders constitute the "book" and specialists are responsible for seeing to it that they are executed when the market reaches the specified limit price. Second, specialists work as facilitators, employing their extensive knowledge of the market in a stock to bring together potential buyers and sellers. Third, specialists serve as dealers when there is insufficient public interest to accommodate willing sellers and buyers at prices reasonably close to the last trade. In these instances, specialists buy for or sell from their own account to improve price continuity and/or depth. (From American stock Exchange, Inc., 1991 Fact Book, Equities and Options, p. 19.)

As a specialist, Taxpayer is required to be a member of the AMEX and its specialist or market maker operation requires, by its very nature, a presence on the floor of the exchange. Giving due consideration to the factors set forth in section 1-3.2(b)(2) of the Article 9-A Regulations, and viewing Taxpayer's activities as a specialist or market maker, such activities in New York State constitute "doing business" within the meaning of section 209.1 of the Tax Law even though Taxpayer does not execute its own trades.

When a corporation is doing business in New York State pursuant to section 209.1 of the Tax Law, such corporation is subject to tax under Article 9-A of the Tax Law.

Accordingly, pursuant to section 209.1 of the Tax Law and section 1-3.2(b) of the Article 9-A Regulations, Taxpayer is subject to the franchise tax imposed under Article 9-A of the Tax Law for all taxable years Taxpayer is doing business in New York State. Taxpayer must compute its tax under Article 9-A pursuant to section 210 of the Tax Law for each taxable year.

DATED: September 23, 1991

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.