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

TSB-A-98(17)C
Corporation Tax
September 16, 1998

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. C980223A

On February 23, 1998, a Petition for Advisory Opinion was received from DJ&J Software, DBA Egghead Computer, 22705 East Mission, Liberty Lake, Washington 99019.

The issue raised by Petitioner, DJ&J Software, DBA Egghead Computer, is whether, under the circumstances presented, it is subject to franchise tax under Article 9-A of the Tax Law and has reporting obligations after it closes its retail stores in New York State.

Petitioner submits the following facts as the basis for this Advisory Opinion.

Petitioner is a retailer of tangible personal property. In the past, Petitioner has generated sales through a variety of different business activities. Petitioner has operated retail stores and sales offices located throughout the United States and Canada, including New York. Petitioner has also employed direct salespeople who solicited sales from corporate, government and educational organizations. These salespeople were based throughout the country and made sales calls to companies in New York. In addition, Petitioner sells its products via mail order and solicits mail order sales primarily through catalogs and other promotional materials which are sent directly to consumers. Mail order sales are also accepted through Petitioner's Internet Web page. All items sold through the mail order division are delivered to customers by common carrier. All orders are accepted at its corporate headquarters, located in another state, and are delivered from inventory stored in a warehouse also in another state. Petitioner is currently registered with New York State for corporate franchise tax purposes.

Petitioner has recently announced plans to close numerous retail stores located throughout the country. Petitioner indicated that it would close all the retail stores that it operates in New York before the end of its fiscal year ending March 31, 1998. Petitioner indicates that it has, in fact, closed these stores. The stores have varying lease termination dates, the longest running lease ends July 31, 1999. Petitioner is currently negotiating with the landlords of the stores scheduled for closing to reach mutually acceptable settlements with respect to the lease termination. If a settlement agreement is reached, Petitioner plans to immediately pay the landlord the agreed upon amount to terminate the lease. Petitioner will not sublease the unoccupied stores if it is unable to reach a settlement agreement with the landlord.

Prior to the closure of it retail stores, Petitioner sold its direct sales division effective May 13, 1996. As a result, Petitioner no longer operates sales offices (other than its corporate headquarters in another state) or employs direct salespeople and has not employed direct salespeople or independent sales representatives since May of 1996. Since that time Petitioner has not had a physical presence in New York other than the retail stores.

Petitioner will continue to operate its mail order business and anticipates that sales into New York may exceed $100,000 on an annual basis. However, these mail order sales will be solicited only through catalogs, similar promotional mailings or via Petitioner's Web page. All mail order sales will be delivered via common carrier or electronically via the Internet.

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.

However, section 1-3.4(b)(9) of the Article 9-A Regulations provides for an exemption from taxation under Article 9-A for corporations which are exempt pursuant to the provisions of Public Law 86-272 (15 USCA §§ 381-384) and states as follows:

> (i) A foreign corporation whose income is derived from interstate commerce is not subject to tax under article 9-A of the Tax Law if the activities of the corporation in New York State are limited to either, or both of the following:
>
> (*a*) the solicitation of orders by employees or representatives in New York State for sales of tangible personal property and the orders are sent outside New York State for approval or rejection; and if approved, are filled by shipment or delivery from a point outside New York State; and
>
> (*b*) the solicitation of orders for sales of tangible personal property by employees or representatives in New York State in the name of or for the benefit of a prospective customer of such corporation if the customer's orders to the corporation are sent outside the State for approval or rejection; and, if approved, are filled by shipment or delivery from a point outside New York State.
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> ...
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> (iv) In order to be exempt by virtue of Public Law 86-272, the activities in New York State of employees or representatives must be 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. Examples of activities performed by such employees or representatives in New York State that are entirely ancillary to the solicitation of orders include:
>
> (*a*) the use of free samples and other promotional materials in connection with the solicitation of orders;

(*b*) passing product inquiries and complaints to the corporation's home office;

(*c*) using autos furnished by the corporation;

(*d*) advising customers on the display of the corporation's products and furnishing and setting up display racks;

(*e*) recruitment, training and evaluation of sales representatives;

(*f*) use of hotels and homes for sales-related meetings;

(*g*) intervention in credit disputes;

(*h*) use of space at the salesperson's home solely for the salesperson's convenience.

(v) Activities in New York State beyond the solicitation of orders will subject a corporation to tax in New York State unless such activities are *de minimis*. Activities will not be considered *de minimis* if such activities establish a nontrivial additional connection with New York State. Solicitation activities do not include those activities that the corporation would have reason to engage in apart from the solicitation of orders but chooses to allocate to its New York sales force. In determining whether a corporation's activities exceed the solicitation of orders, all of the corporation's activities in New York State will be considered. Examples of activities which go beyond the solicitation of orders include:

(*a*) making repairs to or installing the corporation's products;

(*b*) making credit investigations;

(*c*) collecting delinquent accounts;

(*d*) taking inventory of the corporation's products for customers or prospective customers;

(*e*) replacing the corporation's stale or damaged products;

(*f*) giving technical advice on the use of the corporation's products after the products have been delivered to the customer.

(vi) Maintaining an office, shop, warehouse or stock of goods in New York State will make a corporation taxable... A corporation will be considered to be maintaining an office in New York State if the space is held out to the public as an office or place of business of

> the taxpayer. For example, a salesperson uses his or her house for business....

Pursuant to section 1-3.4(b)(9) of the Article 9-A Regulations, a corporation is not subject to tax in New York State if it is exempt pursuant to the provisions of Public Law 86-272. To be exempt pursuant to Public Law 86-272, a corporation's activities in New York State must be limited to the solicitation of orders by employees or representatives in New York State for sales of tangible personal property and the orders are sent outside New York State for approval or rejection; and if approved, are filled by shipment or delivery from a point outside New York State. Activities that exceed the solicitation of orders will subject a corporation to tax in New York State, unless they are *de minimis*. Activities are not *de minimis* if they establish a nontrivial additional connection with New York.

The leasing of retail space in New York is an activity that exceeds the solicitation of orders. 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....

However, there are situations where the ownership of property in New York is not sufficient in magnitude to subject a foreign corporation to tax. It has been held that a foreign corporation which ships raw materials or partially finished goods to an unrelated contractor in this state, by whom the goods are processed or finished, is not taxable solely because of the ownership of such property in New York, assuming that the contractor returns the goods to the foreign corporation or ships them to another contractor outside the state. American Association of Advertising Agencies, Inc., Adv Op St Tax Comm, November 7, 1980, TSB-H-80(32)C.

Also, a foreign corporation manufacturing aluminum, is not subject to tax because it only has minimal ownership of property in New York when it ships its by-product, dross, to a processor in New York who reclaims some aluminum from the dross and then ships the reclaimed metal back to the foreign corporation and disposes of the waste product. Aluminum Company of Canada, Ltd., Adv Op St Tax Comm, August 12, 1983, TSB-A-83(9)C.

In Cargill Financial Services Corporation, Adv Op Comm T & F, September 26, 1990, TSB-A-90(20)C, the petitioner was engaged in the business of trading in stocks, bonds, currencies, commodities and other financial instruments on various exchanges in New York City. The transactions were executed by independent brokers. The opinion held that such activity by itself was not sufficient to deem the petitioner to be doing business in New York State. The petitioner proposed to also trade in commodity futures contracts in precious metals on the

floor of Commodity Exchange, Inc. in New York City. Because of market conditions, it may be prudent for the petitioner to occasionally take title to the precious metal for a short period of time. The physical commodities would be held in warehouses or vaults in New York City. The opinion also held that the when the petitioner occasionally takes title to the precious metal for short periods of time, such ownership of property in New York State is minimal, and if the petitioner is not otherwise doing business in New York, the petitioner would not be taxable under Article 9-A of the Tax Law. However, the actual determination of whether the petitioner was subject to tax was a factual matter dependent on the totality of the corporation's circumstances and not susceptible of determination in an Advisory Opinion.

In this case, after Petitioner closed all of its retail stores in New York State, Petitioner continues to operate its mail order business. These mail order sales will be solicited only through catalogs, similar promotional mailings or via Petitioner's web page. All mail order sales will be approved outside New York State and will be delivered via common carrier or electronically via the Internet. However, until Petitioner reaches agreements with its landlords to terminate its leases for the space occupied by the closed retail stores, Petitioner will continue to have unoccupied leased real or personal property in New York. Petitioner states that it will not sublease the unoccupied leased property in New York.

Pursuant to Public Law 86-272, after Petitioner closed its stores in New York State, Petitioner's mail order business will constitute the solicitation of orders for sales of tangible personal property, but the leasing of retail space in New York State, even when unoccupied, is an activity that exceeds the solicitation of orders. However, in this case, Petitioner will continue to lease the unoccupied retail space in New York only until it can terminate its leases with its landlords. Petitioner is currently negotiating with its landlords to reach termination settlements with them, and will not sublease the unoccupied property. The longest lease ends July 31, 1999. Under these particular circumstances, it is the Department's position that the leased real or tangible property in New York is *de minimis* and is not sufficient to subject Petitioner to tax pursuant to section 1-3.2(d) of the Article 9-A Regulations. Therefore, pursuant to section 1-3.4(b)(9) of the Article 9-A Regulations and Public Law 86-272, after Petitioner closed its retail stores in New York State, Petitioner is exempt from franchise tax under Article 9-A of the Tax Law. Petitioner's tax year under Article 9-A ended on the day it closed its last store in New York, and it must file a report for such taxable year.

DATED: September 16, 1998

/s/
John W. Bartlett
Deputy Director
Technical Services Bureau

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