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ALJ HOLDS NYS REAL ESTATE TRANSFER TAX CANNOT BE IMPOSED ON SALE OF 45% MEMBERSHIP INTEREST IN LLC

By Kara M. Kraman

In an issue of first impression under the New York State real estate transfer tax, a New York State Administrative Law Judge has held that the transfer tax cannot be imposed on a member's sale to its co-member of a 45% membership interest in a limited liability company ("LLC") owning real property in New York State, where both members previously owned the real property as tenants-in-common. *Matter of GKK 2 Herald LLC*, DTA No. 826402 (N.Y.S. Div. of Tax App., May 26, 2016). At issue was the scope of the Department of Taxation and Finance's authority to aggregate acquisitions of minority economic interests in real property.

Facts. The facts in the case were undisputed. In 2007, GKK 2 Herald LLC ("GKK") and an unrelated party ("Co-Owner") acquired an office building located in Herald Square (the "Office Building"). Upon acquisition, GKK and Co-Owner held undivided 45% and 55% tenant-in-common fee interests respectively in the Office Building. New York State real estate transfer tax ("RETT") was paid on that acquisition.

On December 22, 2010, GKK contributed its 45% fee interest to Owner LLC, a newly formed Delaware LLC, and Co-Owner contributed its 55% fee interest to Owner LLC. In exchange, GKK received a corresponding 45% membership interest and Co-Owner received a corresponding 55% membership interest in Owner LLC. GKK and Co-Owner filed RETT returns, reporting the contribution of their fee interests in exchange for membership interests in Owner LLC as exempt "mere changes of identity or form of ownership" under Tax Law § 1405(b)(6).

On the same day, GKK then sold its 45% membership interest to Co-Owner. GKK and Co-Owner timely filed an RETT return, reporting Co-Owner's purchase of GKK's 45% membership interest in Owner LLC as a non-taxable transfer of less than a controlling interest in an entity that owns real property. As a result, Owner LLC became sole owner and operator of the real property, with Co-Owner as its sole member.

The Department claimed that the transaction was a transfer of a 100% controlling economic interest in real property, 55% of which was a nontaxable "mere change in form" of ownership, and 45% of which was

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a taxable change in beneficial ownership, and assessed RETT on that basis.

Applicable RETT law and positions of the parties. RETT is "imposed on each conveyance of real property or interest therein" located in New York State. Tax Law § 1402(a). A "conveyance" is defined to include the transfer or acquisition of a "controlling interest" in an entity that owns real property. Tax Law § 1401(e). In the case of a non-corporate entity, a "controlling interest" is defined as "fifty percent or more of the capital, profits or beneficial interest in such partnership, association, trust or other entity." Tax Law § 1401(b)(ii). The regulations further provide that, "where there is a transfer or acquisition of a controlling interest in an entity . . . and the real estate transfer tax is paid on that transfer or acquisition and there is a subsequent transfer or acquisition of an additional interest in the same entity," the transfers or acquisitions may be aggregated if they occur less than three years apart. 20 NYCRR § 575.6(d). RETT does not apply to "[c]onveyances to effectuate a mere change of identity or form of ownership or organization where there is no change in beneficial ownership." Tax Law § 1405(b)(6).

The Department did not contest that the contributions by GKK and Co-Owner of their respective 45% and 55% fee interests in the Office Building, in exchange for corresponding membership interests in Owner LLC, were exempt from the RETT as "mere change[s] of identity or form of ownership." The Department instead argued that the regulations permitting aggregation of certain acquisitions allowed it to aggregate Co-Owner's purchase of GKK's 45% interest in Owner LLC with Co-Owner's 55% membership interest in Owner LLC, which it acquired in the preceding "mere change in form" transaction. GKK maintained that the sale of its 45% membership interest was a nontaxable transfer of a less-than-controlling interest in real property and that the Department could not aggregate exempt transfers with non-exempt transfers to reach a taxable result.

ALJ Decision. The ALJ held in favor of GKK that Co-Owner's purchase of GKK's 45% interest in Owner LLC was not an acquisition of a "controlling interest" in real property, and no transfer tax was due. She rejected the Department's claim that an acquisition of a 55% interest in an entity that qualified for the "mere change in form" exemption could be aggregated with the acquirer's subsequent purchase of a 45% interest in the same entity.

The ALJ held that the RETT regulation authorizing aggregation does not permit the aggregation of a nontaxable mere change in form transaction with a transfer of a minority interest. She found that the plain language of the regulation (20 NYCRR § 575.6(d)) permitting the aggregation of less than a controlling interest only applied to interests on which RETT was paid on the initial transaction. Therefore, the ALJ concluded that where, as here, no transfer tax was paid on the initial "mere change in form" transaction, the aggregation regulation did not apply. The ALJ also noted that it was not clear that the RETT statute authorized the regulation permitting aggregation of successive transfers at all but found it unnecessary to address that issue, because the regulation did not apply to the transaction at issue.

The ALJ held that the RETT regulation authorizing aggregation does not permit the aggregation of a nontaxable mere change in form transaction with a transfer of a minority interest.

Although the Department argued that the ALJ should defer to its interpretation, the ALJ held that where, as here, the Department's interpretation is inconsistent with the plain language of the statute and regulations, that interpretation is not entitled to any deference. The ALJ also rejected the Department's reliance on precedent under the former real property transfer gains tax, noting that the gains tax statute was broader in scope than the RETT law with respect to aggregation. As we went to press, the Department requested an extension of time to appeal the ALJ decision.

GKK was represented by Irwin M. Slomka, Thomas P. McGovern, and Kara M. Kraman of Morrison & Foerster LLP.

Additional Insights

The ALJ decision calls into question an earlier 2015 New York City ALJ decision that involved the same transaction. In *Matter of GKK 2 Herald LLC*, TAT(H) 13-25 (RP) (N.Y.C. Tax App. Trib., Admin. Law Judge Div., Apr. 1, 2015), a New York City ALJ reached the opposite result, upholding the City's imposition of real property transfer tax ("RPTT") on the transaction. The City ALJ upheld application of the federal income tax "step transaction doctrine" to, in effect, treat the transaction as if GKK sold its 45% fee interest directly to Co-Owner, even though Owner LLC, and not Co-Owner, thereafter owned the fee interest. An appeal of the City ALJ decision is currently pending before the City Tax Appeals Tribunal.

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NYC TRIBUNAL HOLDS THAT HMOs ARE NOT INSURANCE CORPORATIONS AND MUST BE INCLUDED IN COMBINED CORPORATE TAX RETURNS

By Irwin M. Slomka

The New York City Tax Appeals Tribunal, reversing an Administrative Law Judge decision, has held that health maintenance organizations are not "insurance corporations" for general corporation tax purposes, and therefore can be included in the combined returns of their parent holding company. *Matter of Aetna, Inc.*, TAT(E)12-3(GC) and TAT(E) 12-4(GC) (N.Y.C. Tax App. Trib., June 3, 2016). The decision addresses the question of what it means to be "doing an insurance business" for New York City tax purposes.

Background. Insurance corporations are not subject to the New York City general corporation tax ("GCT"). Although prior to July 1, 1974, an insurance corporation was subject to the former City insurance corporation tax ("insurance tax"), effective July 1, 1974, the insurance tax was repealed. The GCT enabling legislation, however, retained an exemption from tax for corporations that were taxable under the repealed insurance tax. Since that time, the Department of Finance has taken the position that an insurance corporation that would have been subject to the former insurance tax is exempt from the GCT. This case involved whether an HMO was an insurance corporation that was "doing an insurance business" in New York, an issue that (somewhat surprisingly) has never previously been addressed for City tax purposes. If it was doing an insurance business, then the HMO could not be included in a combined GCT return.

Facts. Aetna, Inc. is a holding company headquartered in Hartford, Connecticut that, during the years in issue (2005 and 2006), owned multiple HMO subsidiaries. There are several HMO "models." Under the "IPA" model, physicians form an organization that represents their interests in negotiating with the HMO regarding fee reimbursement and other matters. IPA physicians generally provide their medical services to the HMO members, although they can also see other patients. Under the "group" model, the HMO contracts with a physician group practice, which sometimes treats only the HMO members.

HMOs make extensive use of primary care physicians, typically general practitioners, to deliver healthcare services and to act as "gatekeepers" in making referrals to specialists. HMOs compensate physicians either based on a pre-arranged fee schedule (for specialists) or based on a fixed amount each month for each patient the physician sees (for general practitioners). In contrast, an indemnity insurer does not contract with physicians and typically pays physicians (or insureds) only 70-80% of the "usual and customary charge" in a geographic area.

Aetna initially filed combined GCT returns that included the HMO subsidiaries. It later filed refund claims, alleging that its HMO subsidiaries were conducting an insurance business and, therefore, should not have been included in its combined returns. The Department of Finance denied the refund claims, and the case proceeded to hearing.

ALJ determination. After a hearing, an ALJ concluded that the HMOs were doing an insurance business in New York and, therefore, could not be included in a combined GCT return for the years in issue. She acknowledged that HMOs have been distinguished from traditional insurers under federal tax law but concluded that a regulatory decision, *Rush Prudential HMO, Inc. v. Moran*, 536 U.S. 355 (2002), represented a significant change. In that case, the U.S. Supreme Court held that the HMO was an insurer and was, therefore, subject to Illinois insurance regulation, which was not preempted by ERISA. The Department appealed the ALJ decision.

Tribunal Decision. The City Tribunal has now reversed that decision, holding that the HMOs were not "doing an insurance business" within the meaning of the GCT enabling legislation. Therefore, the Tribunal held that the HMOs must be included in their parent holding company's combined GCT returns and that the Department properly denied Aetna's resulting refund claims.

In the absence of a definition of the phrase "doing an insurance business in this state"—the operative phrase for being exempt from the GCT—the City Tribunal looked principally to New York State law, specifically Insurance Law § 1101 ("doing an insurance business") and § 1102(a) (licensing requirement for insurers that "do an insurance business in this state"). The Tribunal noted that those provisions do not apply to HMOs, which are subject to regulation under a different New York statute, Public Health Law Article 44.

The City Tribunal cited several provisions in the Insurance Law that distinguish "insurers" from HMOs and concluded that the ALJ erred in relying on authorities beyond that law and from other states in interpreting the phrase "doing an insurance business." According to the Tribunal, the ALJ erred

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in not adequately considering that Insurance Law § 1109(a) generally excluded HMOs from the reach of the Insurance Law.

The City Tribunal also disagreed with the ALJ's reliance on two opinions of counsel issued by the New York State Insurance Department, one from 1991 and the other from 2004, questioning their legal underpinning as well as their legal effect. With regard to the impact of the U.S. Supreme Court decision in *Rush Prudential*, the Tribunal found it irrelevant in interpreting the intent of the New York State Legislature as to whether HMOs were doing an insurance business. On the other hand, the Tribunal gave "significant weight" to an Advisory Opinion issued by the Department of Taxation and Finance (*Petition of KPMG Peat Marwick*, Advisory Opinion, TSB-A-93(4)C (N.Y.S. Dep't of Taxation & Fin., Jan. 12, 1993)), which concluded that a business conducted by an HMO in compliance with Article 44 of the State Public Health Law was not considered an insurance business.

Finally, the City Tribunal faulted the ALJ for dismissing the significance of amendments to the State Tax Law in 2009 in which HMOs were explicitly redefined as taxable "insurance corporations." The Department had argued that, if HMOs were truly "doing an insurance business" in New York prior to 2009, there would have been no need to specifically refer to them in the 2009 amendments. According to the Tribunal, it was notable that, following those amendments, neither the Insurance Law nor the Public Health Law was amended to eliminate the exclusion of HMOs from the scope of the Insurance Law.

Additional Insights

It is unusual to read a decision directly interpreting the scope of a New York legislative enactment that took place more than 40 years ago. The City Tribunal's decision, which is subject to appeal by Aetna, represents a significant departure from the ALJ's analysis in interpreting the phrase "doing an insurance business." The underpinning of the Tribunal's conclusion is principally that HMOs are distinguished from insurers under the State Insurance Law and Public Health Law, making it unnecessary to look elsewhere in determining whether HMOs are "doing an insurance business." Somewhat surprisingly, the Tribunal does not discuss at all the federal income tax treatment of HMOs—particularly whether they are treated as "insurance corporations" for tax purposes—suggesting that it did not consider such tax treatment significant in interpreting whether they were doing an insurance business.

STATE TRIBUNAL FINDS MATERIAL FACT ADMITTED DUE TO DEPARTMENT'S LATE-FILED ANSWER

By Hollis L. Hyans

The New York State Tax Appeals Tribunal has held that a fact alleged in a petition was deemed admitted by the Department of Taxation and Finance, since the answer denying that fact was not timely filed, and has remanded the case to the Administrative Law Judge for further proceedings. *Matter of Forest City Enterprises, Inc.*, DTA No. 825157 (N.Y.S. Tax App. Trib., May 19, 2016).

Background. Forest City Enterprises, Inc. ("Forest City") is a developer, owner, and operator of urban real estate projects, and has conducted project development activities in New York State through a wholly owned subsidiary, Forest City Ratner Companies, LLC ("FCRC") that had its headquarters in Brooklyn, New York. FC Yonkers Associates, LLC ("FC Yonkers") is another related entity that was formed to own and develop a project known as "Ridge Hill" in Yonkers, New York, on an 80-acre parcel of land. In 2002, the Ridge Hill property was designated as within the boundaries of the Yonkers Empire Zone. After a series of transactions concerning the ownership and management of the Ridge Hill property, FC Yonkers entered into a "Tax Benefit Leaseback Agreement" on August 2, 2007, with the City of Yonkers Industrial Development Agency ("YIDA"), in which FC Yonkers conveyed a leasehold interest in the real property, buildings, and equipment at Ridge Hill (the "Facility") to YIDA, YIDA leased the Facility back to FC Yonkers for rent of $1.00 per year, and FC Yonkers agreed to make certain specified real property tax payments. In January 2008, the City of Yonkers and FC Yonkers executed a "Memorandum of Understanding" in which the parties agreed that FC Yonkers was "legally responsible for making payment-in-lieu-of tax payments to the City of Yonkers" pursuant to a "1979 PILOT Ordinance." In 2008, FC Yonkers paid approximately $7 million to the City of Yonkers in response to an invoice that referenced the Tax Benefit Leaseback Agreement.

For 2008, FC Yonkers claimed an EZ wage tax credit of $3,000 and a QEZE credit for real property taxes of $7 million. On its 2008 form IT-606 (Claim for QEZE Credit for Real Property Taxes), FC Yonkers reported varying numbers of employees during each quarter of 2008, a test year employment number of zero, and a current tax year employment number of one.

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The Audit and the Law. The Department audited the claim for credit, questioning particularly whether FC Yonkers, rather than other related entities, actually employed the individuals it had claimed as employees. There was no dispute that, if the credit was available, Forest City was entitled to claim it due to its ultimate ownership of FC Yonkers, an LLC. Substantial information was produced concerning various employees, their duties with FC Yonkers and related entities, and their various tax filings.

The QEZE credit for real property tax is determined by computing "the product of the benefit period factor..., the employment increase factor and the eligible real property taxes paid or incurred by the QEZE during the taxable year." Tax Law § 15(b)(1). Therefore, the critical issue in the audit was whether FC Yonkers had an "employment number," as defined in Tax Law § 14(g), of at least one for 2008, so that it would have an "employment increase factor" greater than zero.

The auditor reviewed the Department's internal databases and concluded that none of the individuals identified as employees was actually employed by FC Yonkers in New York State. Therefore, the auditor took the position that FC Yonkers' "employment number" was zero for the 2008 year, so that its employment increase factor was also zero, and the entire credit was disallowed.

[U]nder the Tribunal's Rules of Practice and Procedure, if an answer is not timely filed and served, "all material allegations of fact . . . shall be deemed admitted." 20 NYCRR § 3000.4(b)(4).

The ALJ Hearing and Decision. On July 30, 2012, Forest City filed a petition with the Division of Tax Appeals seeking review of the denial. In its petition, Forest City included an allegation that FC Yonkers "has an 'Employment Number' (as that term is defined in § 14 (g) of the New York Tax Law) of at least 1.0 for the Taxable Year." The Division of Tax Appeals acknowledged receipt of the petition on August 10, 2012, commencing the Department's 75-day period to file its answer, which made the answer due on October 24, 2012. On August 17, 2012, the Division of Tax Appeals granted the Department's request to extend the deadline for serving its answer to November 8, 2012. The answer was mailed to the Division of Tax Appeals on November 16, 2012. The answer was received on November 19, 2012, and there was no indication in the Division of Tax Appeals' file that the answer was filed on any earlier date.

In its hearing memorandum, which under the Tribunal Rules of Practice and Procedure is due 10 days before the hearing, the Department raised an alternative basis for its denial of the QEZE credit, claiming that the $7 million payment made by FC Yonkers did not qualify as "eligible real property taxes" for purposes of the QEZE credit.

At the hearing before the ALJ, Forest City presented considerable evidence concerning its employees, including testimony and affidavits, expense receipts, minutes of meetings regarding construction management for the Ridge Hill project, and evidence concerning a claimed common paymaster agreement. Forest City also argued that, because the Department's answer was served late, all factual allegations in the petition were deemed admitted, including the allegation that FC Yonkers had an employment number "of at least 1.0."

The ALJ acknowledged that Forest City was claiming that, since the Department's answer was served late, all material allegations of fact in the petition were deemed admitted. However, she concluded that the assertion that FC Yonkers had an employment number of at least 1.0 was not a material allegation of fact, but rather an "ultimate conclusion of law," and therefore was not deemed admitted by the late-filed answer. The ALJ then reviewed the evidence presented at the hearing and found it insufficient to establish that FC Yonkers employment number was anything other than zero, concluding that there was no common paymaster agreement established, and that Forest City had failed to prove a common law employment relationship between FC Yonkers and the individuals alleged to be its employees. Therefore, the ALJ concluded that FC Yonkers, with an employment number and thus an employment increase factor of zero, was not entitled to the credit and that the issue of whether the taxes themselves were eligible was rendered moot.

Tribunal Decision. The Tribunal reversed the ALJ's conclusion on the preclusive effect of the late-filed answer. It noted that, under the Tribunal Rules, if an answer is not timely filed and served, "all material allegations of fact . . . shall be deemed admitted" 20 NYCRR § 3000.4(b)(4). While recognizing "the vexing nature of the distinction between questions of fact and questions of law," as described in *Pullman-Standard v. Swint*, 456 U.S. 273, 288 (1982), the Tribunal found that, in this case, "the scale tips in favor of a conclusion that the allegation is predominately factual." Since it was undisputed that the question of FC Yonkers employment number was material, the contention was found to be a material allegation and was deemed admitted.

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The only remaining issue was whether the amounts paid by FC Yonkers were for eligible real property taxes under the statute. Since the ALJ had not reached this issue, finding it moot, the Tribunal remanded the case back to the ALJ for a supplemental determination to be made "as expeditiously as possible," and based upon the factual record already made at the hearing.

Additional Insights

It is rare to see a case where the Department's late filing of an answer results in the deemed admission of a material fact, much less one that is so critical to the ultimate determination. Nonetheless, the Tribunal's rules clearly provide for such a result, and the allegation in question—that FC Yonkers has an employment number of at least 1.0—certainly appears to be primarily a factual allegation and could hardly have been more material to the issues in dispute. This decision is an important reminder that the Tribunal's rules and time requirements are to be taken seriously by all parties. On remand, the only issue remaining is whether the taxes paid by FC Yonkers meet the statutory requirements, since the Tribunal's decision has foreclosed further consideration of the employment number issue.

FINANCIAL CORPORATION CAN APPORTION INCOME BECAUSE IT DOES BUSINESS IN NEW JERSEY AT THIRD-PARTY FACILITY

By Irwin M. Slomka

The New York State Department of Taxation and Finance has issued an Advisory Opinion concluding that a financial corporation in New York that conducted certain essential business activities in New Jersey at a third party's "hosting center" is considered to be "doing business" in New Jersey and therefore may apportion some of its income outside the State under the former New York State bank tax. *Advisory Opinion*, TSB-A-16(3)C (N.Y.S. Dep't of Taxation & Fin., May 27, 2016). The Department applied the same "doing business" rules as are used to determine whether an out-of-State corporation is doing business *in New York*.

Facts. A wholly owned financial subsidiary of a global corporate group had its principal office in New York, and all of its employees were based in the State. It principally provided settlement services to large financial institutions throughout the world to mitigate settlement risk from one party to a financial transaction failing to pay what it owes. Beginning in 2004, the subsidiary ("Settlement Provider") entered into a "hosting agreement" with a third-party provider under which the subsidiary was supplied with hosting space and related services at a hosting center in Secaucus, New Jersey.

[T]he Department concluded that having employees travel to the [New Jersey] hosting center on average more than once a week meant that the corporation was doing business in New Jersey.

During the years in issue (2008 and 2009), Settlement Provider maintained some of its data processing equipment at the hosting center. Its New York employees, together with employees of an overseas affiliate, monitored its settlement service on a daily basis. From time to time, its employees performed that monitoring function at the Secaucus hosting center using its data processing equipment maintained there. The on-site employee responding to a settlement exception would, among other things, contact the relevant parties and verify that the necessary "pay-in" funding for the settlement had, in fact, occurred.

In 2008, at least five of the Settlement Provider's employees traveled regularly to the Secaucus hosting center making approximately 60-70 trips. During 2009, a single employee made approximately 50 trips to the hosting center. Settlement Provider was subject to former Article 32 in 2008 and 2009, but also filed New Jersey franchise tax returns for those years.

Advisory Opinion. The issue presented was whether the Settlement Provider was "doing business" in New Jersey so as to be entitled to apportion its income under former Article 32 ("bank tax"). Under the bank tax, a banking corporation must "carry on" business outside New York State in order to apportion its income outside the State by formula. Former Tax Law § 1454(b)(1). The Department ruled that Settlement Provider was doing business in New Jersey because of the nature and frequency of its employees' trips to New Jersey, its long-term license to use the hosting center space, and its maintenance of computer equipment at the hosting center. Therefore, Settlement Provider was allowed to apportion its income for bank tax purposes.

Under the bank tax regulations, the statutory term "business carried on" for apportionment purposes means "doing business" as defined under 20 NYCRR § 16-2.7 (definition of "doing business"). Thus, the same factors used to determine whether a corporation is doing business in New York—*e.g.*, the nature, continuity, frequency, and regularity of its activities—are used to determine whether

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the corporation is carrying on business outside the state for apportionment purposes.

The Department ruled that the conduct by Settlement Provider's employees at the Secaucus hosting center in resolving potential transaction errors was critical to its successful functioning as a financial institution and was sufficient proof that it was carrying on business outside the State in New Jersey. The Department also relied on Article 9-A precedent since the "doing business" criteria in Article 9-A and former Article 32 are substantially the same.

The fact that the hosting center was not a bona fide office or branch of the Settlement Provider did not change the result. Rather, the Department concluded that having employees travel to the hosting center on average more than once a week meant that the corporation was doing business in New Jersey. Also relevant was the fact that the corporation had the right to use the hosting space for a 10-year period (evidencing continuity), as well as the fact that the Settlement Provider maintained its own equipment there. The Department did not, however, rule on how much of the Settlement Provider's income could be apportioned outside the State.

Additional Insights

The Advisory Opinion is not surprising given the bank tax regulations, which expressly apply the "doing business" nexus standards in determining whether a banking corporation is "carrying on" business outside the State. Although the Advisory Opinion addressed the right of a banking corporation to apportion its income, it is also a reminder of the broad scope of the New York nexus rules, even prior to corporate tax reform. Thus, having access to space in New York—even if, as here, not pursuant to a formal lease—and regularly sending employees into the State to perform critical business functions will typically result in taxable nexus with New York.

DEPARTMENT ADVISES THAT PROVIDING ADVERTISERS WITH INFORMATION ABOUT INTERNET USERS IS A TAXABLE INFORMATION SERVICE

By Hollis L. Hyans

The New York State Department of Taxation and Finance has advised that the provision of data mined from the Internet to advertisers is the provision of a taxable information service and is not exempt as "personal or individual in nature." *Advisory Opinion*, TSB-A-16(18)(S) (N.Y.S. Dep't of Taxation & Fin., May 5, 2016).

Facts. The Petitioner provides a service that makes information about groups of individual Internet users available to its customers, who then provide advertisements to each individual user in the group. The Petitioner collects data by paying chosen sets of websites to place a small piece of computer code, known as an HTML tag, on selected pages, each of which generates a "cookie" when a user interacts with that website. That cookie collects data about the website and the "End-Users," and becomes associated with an End-User's Internet browser so it can continue to collect new information about subsequent behavior of the End-User as he or she travels to other websites.

The Petitioner collects and generates specific and unique data about the Internet usage of the End-Users and segments the data into a useable format for its customers. All segments are created specifically for advertisers to target with advertising. Petitioner's customers then make the segments available to their clients for ad targeting. Each customer can select its mix of segments, and, potentially, each customer could receive a different mix of data. The segments are created exclusively by Petitioner, but approximately 5% come from offline data providers, collected from a source other than on the Internet or any other digital source, such as data collecting by TV ratings companies about viewing habits.

Petitioner's customers use the service to deliver targeted online advertisements gathered via cookies about End-Users' visits to websites. The cookies and the data have variable useful lives and decrease in value over time, so up-to-date information is most valuable to Petitioner's customers. For example, hotels may want to reach an End-User who has purchased an airplane ticket as quickly as possible, so it is important that information about the End-User be promptly available. Petitioner generates information gathered via hundreds of billions of cookies each month.

Advisory Opinion. Without any discussion or analysis, the Department concluded that Petitioner's service is a taxable information service under Tax Law § 1105(c)(1), which imposes sales tax on receipts from the service of "furnishing [ ] information …. including the services of collecting, compiling, or analyzing information of any kind or nature and furnishing reports thereof…." It then also concluded that Petitioner's service was not exempt as "personal or individual in nature" and not "substantially incorporated in reports furnished to other persons,"

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because the information is not "'uniquely personal.'" In reliance on cases such as *Allstate Ins. Co. v. Tax Comm'n*, 115 A.D. 2d 831 (3d Dep't 1985), and *Matter of ADP Collision Estimating Services, Inc.*, DTA No. 804973 (N.Y.S. Tax App Trib., Aug. 8, 1991), the Department found that information is not "uniquely personal or individual in nature" if it comes from a common source that is not itself confidential. Since most of the information about End-Users was collected by Petitioner from providers who can sell the same information to others, the information was found not to be uniquely personal, even though no two customers will get exactly the same information, with the Department noting that, even where it was found to be a "virtual mathematical impossibility" for customers to receive duplicate information, the service was held by the courts to be insufficiently personal or individual to be exempt. *Rich Products Corp. v. Chu*, 132 A.D.2d 175, 177 (3d Dep't 1987).

Additional Insights

This Advisory Opinion is consistent with the increasingly narrow parameters that have been drawn by the courts and the State Tax Appeals Tribunal on the category of information that will be regarded as personal or individual in nature. Although not mentioned in the Advisory Opinion, two decisions issued just a few months ago by the Tribunal held that, as long as the source of the information being furnished is publicly available, it does not matter that the data was not obtained from a common database or that it was not substantially incorporated into reports furnished to other customers. *Matter of RetailData, LLC*, DTA No. 825334 (N.Y.S. Tax App. Trib., Mar. 3, 2016); *Matter of Wegmans Food Markets, Inc.*, DTA No. 825347 (N.Y.S. Tax App. Trib., Mar. 10, 2016) (*see* discussion in the April issue of *New York Tax Insights*).

NEW COMMISSIONER APPOINTED TO STATE TAX APPEALS TRIBUNAL

Dierdre K. Scozzafava has been confirmed as a Commissioner of the New York State Tax Appeals Tribunal, filling a vacancy left by former Commissioner Charles H. Nesbitt. She joins President and Commissioner Roberta Moseley Nero and Commissioner James H. Tully, Jr. Ms. Scozzafava previously served as New York Deputy Secretary of State for Local Government and as a representative in the New York State Assembly. We extend our best wishes to Commissioner Scozzafava in her new position.

INSIGHTS IN BRIEF

Purchase of Sculpture in Germany Initially Loaned to an Exempt Museum in New York City is Not Subject to Sales Tax

The purchase by a Florida limited liability company from a New York-based art dealer of a sculpture created in Germany, which the purchaser first loaned to a tax-exempt museum in New York City before having it delivered in Florida, is not subject to New York State and local sales tax. *Advisory Opinion*, TSB-A-16(17)S (N.Y.S. Dep't of Taxation & Fin., May 2, 2016). The Department of Taxation and Finance concluded that where the purchaser authorized the museum to retrieve the sculpture from the fabricator in Germany, and the museum contracted with a contract carrier (and not a common carrier) to do so, physical possession was deemed to take place in Germany. In addition, no sales tax was due on the purchaser's loan of the sculpture to the museum, because the museum took delivery outside New York State.

Auto Body Repairs Performed Outside New York on Vehicles Delivered in New York Are Subject to Sales Tax

Where the operator of a New York auto sales showroom also maintains an auto body shop in New Jersey to perform repairs on customers' damaged vehicles, the charges for auto body repairs are subject to New York State and local sales tax, even though the work is performed in New Jersey. *Advisory Opinion*, TSB-A-16(16)S (N.Y.S. Dep't of Taxation & Fin., Apr. 28, 2016) (released June 2016). Charges for taxable repairs or other taxable services are subject to sales tax where the repaired or serviced property is delivered to a customer in New York. Since all vehicles on which repairs are made are delivered to customers at the New York auto sales showroom, the Department of Taxation and Finance ruled that sales tax will apply to the repair charges.

Audit Methods Held to Be Unreasonable

In *Matter of Metropolitan Minimart Corp* and *Matter of Ahmed Issa*, DTA Nos. 826155 & 826156 (N.Y.S. Div. of Tax App., May 26, 2016), a New York State Administrative Law Judge held that the audit methods relied upon in a sales and use tax audit were not reasonable, that the audit therefore lacked a rational basis and that the notices of determination should be canceled. The business in question was described as a "typical New York City bodega" selling grocery items, and its records were found inadequate to permit an audit, so that resort to an external index was appropriate. However, the ALJ rejected the auditor's reliance on a Restaurant Industry Operations

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Report applicable to limited service restaurants and what was described as the auditor's "unwavering' position that the business was similar to a Subway, noting that, unlike a Subway, the bodega accepted food stamps, did not have ovens, did not sell hot meals, and sold many grocery items. The ALJ also rejected the auditor's use of a "utility factor" based on limited service restaurants, noting that the bodega had no energy-driven appliances, such as ovens and cook tops, making the use of the utility factor particularly unreasonable.

Data Storage Charges Not Subject to Sales or Use Tax

The New York State Department of Taxation and Finance has issued advice finding that a web-based data-hosting service's charges for cloud storage space are not subject to sales or use tax. *Advisory Opinion*, TSB-A-16(19)S (N.Y.S. Dep't of Taxation & Fin., May 20, 2016). The Department found, first, that the charges were not receipts from the sale of software, since the software involved was available to all users without charge, and second, that the service was not the provision of a taxable information service, since customers can access only their own information, which they have stored using Petitioner's service. Finally, the Department found that the Petitioner was not storing tangible personal property, which would be taxable under Tax Law § 1105(c)(4), nor performing any of the other enumerated services that are subject to tax.

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