

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

TSB-A-09(64)S
Sales Tax
December 2, 2009

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S090309A

On March 9, 2009, the Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED].

The issue raised by Petitioner is whether disbursements made by Petitioner to a tenant in accordance with provisions included in a lease agreement, as described below, are subject to sales or use tax. It is concluded that these disbursements are not payments for the sale of tangible personal property or services, and are not subject to sales or use tax.

Facts

Petitioner owns a building in New York City. Petitioner leases space in the building to a commercial tenant (Tenant). The leased premises have been stripped bare, to the concrete subfloor and steel beams.

Tenant is authorized under the lease agreement to make “alterations, installations, improvements, additions or other physical changes” (Alterations) to the leased premises, subject to Petitioner’s prior consent. Alterations must be made in accordance with the plans and specifications approved by Petitioner. Alterations that require Petitioner’s consent must be performed under the supervision of an architect approved by Petitioner, and must be performed by contractors and subcontractors either designated or approved by Petitioner. For “Initial Alterations” (i.e., Alterations made to prepare the leased premises for Tenant’s initial occupancy), the lease identifies an architect and a number of contractors that Petitioner approves.

Petitioner is required under the lease agreement to contribute to a “Tenant Fund” that is intended to reimburse Tenant for certain costs incurred by Tenant in performing Initial Alterations. The lease sets up a mechanism for Petitioner to pay or make disbursements of the Tenant Fund to Tenant for these costs, which disbursements are not to exceed a specified amount of approximately \$ 1 million, with Tenant paying “the amount of any excess of the cost of the Initial Alterations over the Tenant Fund.” The Initial Alterations to the leased space will be the property of Petitioner to the extent that the Tenant Fund is used by Tenant to perform the alterations, subject to Tenant’s right to use the alterations during the lease term. We are not asked, and do not opine, about the tax treatment of Initial Alterations paid for by Tenant.

Analysis

In order for the disbursements from the Tenant Fund in this case to be subject to sales tax, the disbursements must constitute receipts from the sale by Tenant to Petitioner of tangible personal property or enumerated taxable services. *See* Tax Law §1105(a) and (c). On the basis of the facts Petitioner provides, Petitioner is not purchasing any property or services from Tenant as a result of making the disbursements. When, as in the present case, (1) a landlord reimburses a tenant for the cost of making improvements to the leased premises, and (2) the improvements contribute significantly to the tenant’s comfort and convenience during a substantial portion of the lease term, but become the landlord’s property after expiration of the lease, the reimbursement does not constitute a taxable transaction between the landlord and tenant for sales tax

purposes. Accordingly, the disbursements in the present case are not receipts from the sale of property or services to Petitioner, and are thus not taxable.

It should be noted that Tenant's purchases of tangible personal property on an uninstalled basis to be incorporated into the Initial Alterations are purchases at retail subject to sales tax under Tax Law §1105(a). Tenant's purchases of tangible personal property and installation services from contractors who construct the Initial Alterations for Tenant are not subject to tax if the Initial Alterations qualify as capital improvements. *See* Tax Law §§1105(c)(3)(iii), 1115(a)(17). If the Initial Alterations remain tangible personal property after installation, then Tenant's purchases of tangible personal property and installation services from contractors for that property are subject to tax under Tax Law §§1105(a) and 1105(c)(3).

DATED: December 2, 2009

/S/

Jonathan Pessen
Director of Advisory Opinions
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NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.