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Property Qualifying for the Investment Tax Credit for the Financial Services Industry

The issue raised by Corporation X is whether the tangible personal property and other tangible property, including buildings and structural components of buildings, purchased for use by certain of the business units, as described below, of Corporation X qualifies for the investment tax credit allowed under section 210.12(b)(i) of the Tax Law for taxable years ending in 1999, in 2000, and in 2001.

The tangible personal property and other tangible property at issue are purchased for use by the following business units of Corporation X: (1) the Investment Banking division, (2) Client Financial Services, (3) the “Electronic Trading” unit, (4) Prime Brokerage, (5) the Operations division, and (6) the Research division. This NYT-G only addresses tangible personal property and other tangible property purchased for use by these business units in the activities described below, and does not address any other tangible property that may be used in other activities by Corporation X.

Substantially all of the nonadministrative staff in each of these six business units are licensed as *Series 7 – General Securities Representatives* (and, in fact, many of the administrative employees working within these divisions have chosen to obtain their individual Series 7 licenses as well.) The Series 7 license is regulated by the National Association of Securities Dealers, Inc. (NASD). Corporation X states that NASD requires any person who is associated with a securities firm and is engaged in the securities business of the firm to register with NASD. Part of that registration process is passing the Series 7 examination, which is administered by NASD. The examination covers federal securities laws, the rules and regulations of the Securities and Exchange Commission (SEC), the NASD rules and regulations, securities products, the operation of financial markets, economic theory and risk, corporate finance, accounting, portfolio analysis, fair sales practices, and tax treatment of investments. In order to take the examination, an individual must be sponsored by a NASD-member brokerage firm (or a self-regulatory organization, exchange, or state regulator.) Corporation X sponsors those of its employees in the six business units at issue, as well as those in other business units, to enable them to obtain the Series 7 license.

The following are descriptions of the six business units at issue.

1. *Investment Banking*

Corporation X’s Investment Banking division engages in underwriting of securities as well as the financial advisory services that support those underwriting activities.

The fundamental underpinning of Corporation X’s Investment Banking services is its ability to implement business strategies through underwriting, such as public offerings and private placements of equity and debt instruments, and other related activities. For example, the Investment Banking division will engage in equity financings in which Corporation X buys

common stock or convertible bonds from an issuer and then resells them to customers. Corporation X typically assumes the risk of buying a new issue of securities from the issuing corporation or government entity and resells them to the investing public either directly or through other dealers, earning its profit on the spread (*i.e.*, the difference between the price paid to the issuer and the public offering price.) The Investment Banking division may also participate in an underwriting syndicate, either as the manager of such syndicate or as a non-managing member that simply purchases blocks of the underwritten securities at a discount and resells them to the investing public.

Corporation X's Investment Banking Division similarly underwrites issuances of investment grade securities, including bonds, preferred stock, and derivatives. As with equity financings, Corporation X earns a spread equal to the difference between the price Corporation X pays and the offering price at which Corporation X's resale is made to the public. Corporation X investment bankers also securitize commercial mortgage debt (by bundling and securitizing the value of outstanding loans) so those securities can be sold to customers and monetize assets (by, for example, creating equity derivatives that can themselves be traded). The Investment Banking division also engages in leveraged financing transactions, such as underwriting junk bonds, syndicating loans, or providing derivative financing through which a client might hedge an outstanding securities issuance, with the offsetting instrument then being marketable to the public.

Corporation X's Investment Banking division also provides related financial advisory services to help plan for the underlying transaction that creates the client's stock or debt capital needs and necessitates Corporation X's underwriting actions as a broker/dealer in the equity or debt markets. Those underlying transactions can include mergers and acquisitions, divestitures (*i.e.*, the orderly distribution of large blocks of a corporation's stock), corporate defense activities, restructurings, and spin-offs. Some of the types of corporate defense strategies that the Investment Banking division helps clients to undertake include targeted repurchases in which a firm buys back its own stock; exclusionary self-tenders, in which a firm makes a tender offer for a given amount of its own stock while excluding targeted shareholders; and "going private" transactions, where the publicly owned stock in a firm is purchased by a private group (typically existing management). Restructurings might involve buying and selling of companies or divisions of companies for cash and issuing or redeeming debt and/or stock to achieve a more optimal capital structure. Corporation X also helps clients evaluate their capital adequacy or debt to capital structure and engage in equity or other financing needed to optimize capital.

Corporation X relies on its broker/dealer expertise in conducting all of these financial advisory services. Whether it is a merger, acquisition, divestiture, or some other restructuring, once such an action has been decided upon, Corporation X will typically carry out the chosen transaction to effectuate the company's stock or debt capital needs.

Corporation X's fees are typically negotiated on a client-by-client basis. There is no standard formula, but the fees generally bear a direct relationship to the value of the securities

involved. Corporation X's fees are often conditioned upon the consummation of a securities transaction. If the transaction upon which Corporation X is advising does not close, Corporation X may receive a reduced fee or no fee at all.

Substantially all of the nonadministrative employees in the Investment Banking business unit are licensed as *Series 7 – General Securities Representatives*.

2. Client Financial Services

Corporation X's Client Financial Services segment counsels individual investors on making new investments or changes in their portfolios and engages in authorized trading, including some discretionary trading, on behalf of customers based on their investment objectives.

Investment professionals in Client Financial Services work with clients to provide investment advisory services and order execution. They execute sales on behalf of clients in the equities and fixed income markets, including, but not limited to, purchases and sales of investment funds. With regard to order execution, employees in Client Financial Services earn fees for engaging in trading for the customer's portfolio on a discretionary basis and also earn commissions for nondiscretionary orders.

Historically, Corporation X and other securities firms charged only for commissions on sales and purchases. In recent years, the custom has been to charge for this service based on the amount managed, although arrangements with particular clients are often separately negotiated. Often, value-based charges are reduced if Corporation X earns significant commissions from trading in the account. In some cases clients may only pay execution charges or commissions rather than advisory fees for Corporation X's Client Financial Services.

Substantially all of the investment professionals in the Client Financial Services business unit are licensed as *Series 7 – General Securities Representatives*.

3. Electronic Trading

The Electronic Trading business unit was established to build a world-class trading system for Corporation X's high-net-worth clients. In creating this unit, Corporation X recognized that through its Internet-based business it would be able to deliver its broker/dealer products and services globally from its New York base of operations. Corporation X recognized a global opportunity to attract clients outside the United States, since the majority of high-net-worth assets at that time were overseas. Corporation X saw itself as well positioned with a leading global presence and sophisticated securities products.

In developing the Electronic Trading business, Corporation X invested in Web site development, operations, and back office systems; investor service center technology; and

workplace tech equipment, primarily purchasing computers and data communications equipment to conduct the Electronic Trading business. This equipment is necessary for the operations of the Electronic Trading segment, including trading processing, recordkeeping, etc., and allowing investment advisors to field calls from investors, provide assistance with trading operations, provide advice, and give customer service.

Electronic Trading had its own management, technology, finance, marketing, compliance and products groups. Two of the larger departments were the technology development department and the infrastructure technology team. Each department consisted of multiple groups carrying out different functions.

The technology development department consisted of the following groups:

- Services group. This group built the on-line trading system capability of Electronic Trading and handled the “front-end” system application that enabled the trading of securities, bonds, treasury bills, mutual funds, IPO shares, etc.
- Order group. This group built the back-end supporting systems by which Electronic Trading orders are handled in Corporation X.
- Client Financial Services group. This group built the call center software used by employees outside New York State. The software enabled a sophisticated system of phone call integration, whereby the system recognizes a phone number from which a call originates and recognizes the account holder so that the employee representative taking the call can more efficiently respond.
- Data architecture group. This group created the Electronic Trading database and access to data sources, including market data, product look-up function (based on stock sticker), etc.
- Operations/Finance group. One of this group’s biggest requirements was to build the on-line account opening system that enabled employees outside New York State to approve account opening documents and establish accounts for users much more quickly than the manual process.
- Content group. This group consisted of a team of individuals that controlled the data sources available on the Electronic Trading platform. The data sources available through the Web site include news reports, various information services, internal Corporation X research pages, and external research resources. External resources include S&P tearsheets, access to EDGAR (SEC) filings, connection to “Big Charts,” access to Reuters news services, etc.
- Client Financial Services Site group. This group handled how investors’ portfolios would be displayed on the Electronic Trading Web site. The on-line portfolios show cash and security balances and a host of other information relative to securities and securities trading.

- Multi services group. This group's functions span across all of the other product groups. This group consulted with all other products groups regarding software design, function, and processes. This Multi services group is responsible for the server layer of the infrastructure upon which the other platforms operate.

The technology infrastructure team also consisted of various groups:

- Production support team. This group worked with the technology development team to develop systems that would enable 24/7 support of the Electronic Trading Web site. They were responsible for building the failover (backup) structure of Electronic Trading and the system to allow continuous monitoring of the site.
- Market data infrastructure. This team was responsible for the market data infrastructure. It governs the market data housed within Electronic Trading.
- Networking infrastructure. This group was responsible for the networking infrastructure and Internet connectivity functions. It was involved in the original hardware purchases for the network design, the firewalls within the systems, and the failover (backup) hardware supporting Electronic Trading.
- Quality Assurance. The Quality Assurance function created a test environment necessary to test the systems before they went to the production stage. This team tested the applications, supported the systems hardware, and helped with the design of the systems. Systems administrators supporting the different servers within Electronic Trading reported to the Quality Assurance team.

The Products group defined what was built into the Electronic Trading platform, writing product specifications and ensuring that the technology and other development groups met the standards they had designated. It designated the functionality of the Web site, including which products it would offer, e.g., on-line trading, the mutual funds it was to contain, etc. It designed the actual Web site, defining how it should look and the functionality to be incorporated. In carrying out its function, it interfaced with the technology development and infrastructure teams that were actually building and supporting the applications, refining and adjusting the products and procedures as they developed.

There are different groups within the Products group. Each of these groups has different responsibilities. For example, one group determines how investors' shares are tracked within their accounts. This group integrates the client "front-end" application with the "back-end" systems relating to the custody of securities held in investors' accounts. It determines how the on-line brokerage statements should look and work. It determines how the cost basis of shares is tracked and recorded for each investor. Other employees in different areas of the Products group designed and maintain the automated account opening process available to Electronic Trading customers. They defined how on-line brokerage statements would look and function and how

trade executions were to be processed and how cost basis would be determined. They designed how the front-end client application would be integrated with the back-end systems.

The Sales business unit consisted of separate groups within Sales that supported different areas. This group handled all marketing functions of the venture. It addressed the best mediums to use to acquire new clients, including news publication advertising, Internet advertising, etc. It defined the client base it wanted to reach; i.e., individual or enterprise, net worth thresholds, etc. The marketing group produced a television commercial promoting the new Electronic Trading Web site and printed up materials for distribution to potential clients. It also made branding decisions, i.e., how it wanted to portray the Corporation X “brand” in the Electronic Trading effort.

The Finance group did all the financial projections for Electronic Trading when the effort was first getting underway. It kept track of sales and fixed and variable costs in all of the other departments. It tracked costs spent on technology, marketing, operations, etc.

Electronic Trading also had employee representatives on the trading desk and employees dedicated to management and human capital functions, legal/compliance and business support services.

The Electronic Trading system was fully operational in 2000 and 2001. At the end of the 2000 taxable year, there were many accounts on the Electronic Trading platform and there were several hundred employees. Millions of dollars had been invested in computers, data communications equipment, and other technology.

4. *Prime Brokerage*

Prime Brokerage acts as the prime broker for various hedge fund clients. Corporation X provides administrative services that support the clients' securities transactions. Often, Corporation X, in addition to entering into an agreement with the client, enters into an agreement with other brokers used by the client.

Corporation X's employees in this segment (licensed under Series 7) compile lists of trades and report the daily transactions of the hedge fund. Prime Brokerage employees monitor the risks of the hedge fund and its margin loan borrowings. Prime Brokerage is also part of Corporation X's Operations function, which supports equity and Fixed Income sales and trading and supports custody clearance.

Corporation X executes trades as directed by the client's broker and sends confirmations either to the broker or to the client, as the client wishes. Corporation X offers access to trading solutions or platforms through various channels. It handles order management, trade execution and multi-currency portfolio accounting. Information is provided to assist investment managers and hedge funds in making purchase and sale decisions.

Through Corporation X, customers are provided securities lending services that give them access to hard-to-borrow securities. Realizing the growing importance and use of technology by clients, Corporation X has developed and implemented key technologies to speed execution and increase the flow of information. In addition to this technology, Corporation X employees continually hone their proprietary trading techniques to ensure customers have ready access to stocks, at the time and in the quantity that they require.

5. Operations

Corporation X's Operations division is responsible for processing, clearing, and settling trades in a timely and accurate manner. It provides integrated and highly secure operations services to several business units within Corporation X. The Operations division is responsible for ensuring that Corporation X has the technological infrastructure, including processes and controls, to support the complex financial transactions in which the firm's traders engage.

For Corporation X's Equities Division, Operations supports various business products including US Shares sales, Equity Derivatives, Equity Portfolio Trading, Equity Capital Markets, Client Services, and many other products.

For Corporation X's Fixed Income division, Operations supports several products including Corporate Debt Sales, Global Interest Rate Products, Currency, Commodities, Municipal Bonds sales, etc.

The Operations division supports the firm's Capital Markets Operations. Whenever a purchase or sale of securities occurs, it must go through a sophisticated clearing and settlement process. The division implements and manages these operations, working closely with the sales and trading functions.

Operations works with the Investment Management Division in providing support for the trading activities of investors. Operations manages the flow of information, including account management and investment performance measurement, that is essential for the Investment Management Division to plan and implement securities trades for its clients.

Operations manages the reconciliation and payment processes both internally between Corporation X departments and externally between Corporation X and banks and exchanges that are necessary for securities trades to be implemented. This process involves managing payments and expenses, reporting, operational oversight and regulatory reporting of securities transactions so that purchases and sales of securities can be implemented in an appropriate and lawful manner.

6. Research

Corporation X's Research department performs a differentiated research effort that is firmly aligned with the interests of Corporation X's investing clients as an important part of its Equities business. Employees of the department engage in global research to enable them to provide industry expertise, independent thinking and timely insights to investors. These researchers are required to obtain their Series 7 licenses.

Applicable law and regulations

Section 210.12 of the Tax Law contains the provisions for the investment tax credit, and provides, in part:

(a) A taxpayer shall be allowed a credit, to be computed as hereinafter provided, against the tax imposed by this article. The amount of the credit shall be the percent provided for herein below of the investment credit base. The investment credit base is the cost or other basis for federal income tax purposes of tangible personal property and other tangible property, including buildings and structural components of buildings, described in paragraph (b) of this subdivision....

* * *

(b)(i) A credit shall be allowed under this subdivision with respect to tangible personal property and other tangible property, including buildings and structural components of buildings, which are: depreciable pursuant to section one hundred sixty-seven of the internal revenue code, have a useful life of four years or more, are acquired by purchase as defined in section one hundred seventy-nine (d) of the internal revenue code, have a situs in this state and are .. (D) principally used in the ordinary course of the taxpayer's trade or business as a broker or dealer in connection with the purchase or sale (which shall include but not be limited to the issuance, entering into, assumption, offset, assignment, termination, or transfer) of stocks, bonds or other securities as defined in section four hundred seventy-five (c)(2) of the Internal Revenue Code, or of commodities as defined in section four hundred seventy-five (e) of the Internal Revenue Code, (E) principally used in the ordinary course of the taxpayer's trade or business of providing investment advisory services for a regulated investment company as defined in section eight hundred fifty-one of the Internal Revenue Code, or lending, loan arrangement or loan origination services to customers in connection with the purchase or sale (which shall include but not be limited to the issuance, entering into, assumption, offset, assignment, termination, or transfer) of securities as defined in section four hundred seventy-five (c)(2) of the Internal Revenue Code.... For purposes of clauses (D) [and] (E) ... of this subparagraph, property purchased by a taxpayer affiliated with a regulated broker, dealer ... is allowed a credit under this subdivision if the property is used by its affiliated regulated broker, dealer ... in accordance with this subdivision. Provided,

however, a taxpayer shall not be allowed the credit provided by clauses (D) [and] (E) ... of this subparagraph unless all or a substantial portion of the employees performing the administrative and support functions resulting from or related to the qualifying uses of such equipment are located in this state....

* * *

(d) A taxpayer shall not be allowed a credit under this subdivision with respect to tangible personal property and other tangible property, including buildings and structural components of buildings, which it leases to any other person or corporation except where a taxpayer leases property to an affiliated regulated broker, dealer ... that uses such property in accordance with clause (D) ... of subparagraph (i) of paragraph (b) of this subdivision. For purposes of the preceding sentence, any contract or agreement to lease or rent or for a license to use such property shall be considered a lease....

Section 5-2.4(c) of the Business Franchise Tax Regulations (Article 9-A Regulations), contains the definition of the term *principally used*, and provides as follows:

The term *principally used* means more than 50 percent. A building or addition to a building is principally used in production where more than 50 percent of its usable business floor space is used in storage and production. Floor space used for bathrooms, cafeterias and lounges is not usable business floor space. Space used for offices, accounting, sales and distribution is not used in production. Dual purpose machinery is principally used in production when it is used in production more than 50 percent of its operating time.

Technical Services Bureau Memorandum entitled *Tax Credits for the Financial Services Industry*, December 1998, TSB-M-98(8)C and (6)I contains the definition of the term *principally used* and provides as follows:

Principally used means more than 50 %. A building or an addition to a building is principally used in qualifying activities where more than 50 % of its usable business floor space is used in qualifying activities. Floor space used for bathrooms, cafeterias, and lounges is not usable business floor space. Equipment is principally used in qualifying activities when it is used in such activities more than 50 % of its operating time. Operating time may be determined based on actual time, cost allocations to individual business units, or any other reasonable method that accurately reflects operating time.

Opinion

The investment tax credit under section 210.12 of the Tax Law was extended to provide new tax credits for the financial services and banking industry by Chapter 56 of the Laws of 1998, which added section 210.12(b)(i)(D), (E), and (F) to the provisions.

Sections 210.12(b)(i)(D) and (E) of the Tax Law contain the principal use requirement of the investment tax credit provisions that must be met by a broker or dealer. Such requirement provides that the tangible property must be principally used in the ordinary course of the taxpayer's business as a broker or dealer *in connection with the purchase or sale (which shall include but not be limited to the issuance, entering into, assumption, offset, assignment, termination, or transfer)* of stocks, bonds, or other securities as defined in IRC section 475(c)(2) or of commodities as defined in IRC section 475(e) or in providing lending, loan arrangement, or loan origination services to customers *in connection with the purchase or sale* of securities as defined in IRC section 475(c)(2). Further, investment advisory services provided by a broker or dealer for a regulated investment company, as defined in IRC section 851, would meet the principal use requirement.

The extension of the investment tax credit to the financial services and banking industry was initially introduced in the State Senate on February 23, 1998, as Bill S.6248. It should be noted that in this bill, section 210.12(b)(i)(D) contained the following language:

principally used in the ordinary course of the taxpayer's trade or business as a broker or dealer or investment advisor in connection with the purchase or sale (which shall include but not be limited to the issuance, entering into, assumption, offset, assignment, termination, or transfer) of stocks, bonds or other securities as defined in section four hundred seventy-five (c)(2) of the Internal Revenue Code, or of commodities as defined in section four hundred seventy-five (e) of the Internal Revenue Code" (emphasis added).

However, when the final bill was enacted as Chapter 56 of the Laws of 1998, the provision adding section 210.12(b)(i)(D) of the Tax Law did not include the phrase "*or investment advisor.*"

The New York State Assembly's Memorandum in Support of Bill A.9094C (Chapter 56 of the Laws of 1998) notes in its summary of provisions that the provision adding section 210.12(b)(i)(D), (E), and (F) "extends the ITC to the financial services and the banking industry for investments in equipment used for security trading practices, including computers and telecommunications technology...." The New York State Senate's Memorandum in Support of A.9094C notes in its summary of provisions that this provision will:

extend the State's Investment Tax Credit, currently offered to manufacturers for investing in tangible property within New York State, to the State's financial services and banking industries. The credit would be made available for those investments in tangible property, including qualifying property held by corporations or individuals either directly or through one or more partnerships engaged in financial services that are similar to the investments that now qualify for manufacturers. Examples include investments in computer and telecommunications technology used for 'assembly line' functions of the securities industry such as trading and other security dealer activities.

Historically, the investment tax credit provisions under section 210.12 of the Tax Law were enacted to encourage the modernization of antiquated production facilities and make New York a more attractive location for manufacturers by giving a tax credit for new investments in buildings, equipment and facilities used for production. (See Governor's Memorandum approving L.1969, Ch. 1072, 1969 NY Legis Ann, at 577.)

The Technical Services Bureau Memorandum entitled *Investment Tax Credit for Computers and Computer-Related Equipment*, May 15, 1987, TSB-M-87(5)C, explains how to determine whether computers and computer-related equipment are principally used in the production of goods and qualify for the investment tax credit under section 210.12 of the Tax Law. In determining whether the investment tax credit is allowed on computers and computer-related equipment, a primary consideration is how the property is used in the production of goods. The term "manufacturing" is generally defined for tax purposes as the production of a new or different article from raw or prepared materials. A particular process must bring about a substantial or significant change in the basic material in order to constitute manufacturing; a superficial change in the basic material does not amount to manufacturing. *Processing* has been defined as the performance of any service on tangible personal property for the owner which effects a change in the nature, shape, or form of the property. A second consideration is to what extent the computer and computer-related equipment are used in the production process, including all applications handled by the computer and the computer-related equipment and the percentage of operating time devoted to each application.

In the *Matter of Epic Chemicals, Inc.*, TSB-H-81(59)C, the taxpayer's computers were used to make mathematical calculations relating to alterations of chemical formulas based upon inventory and cost factors to keep manufactured products within quality and profitability parameters. The computers were primarily used to aid in the making of management decisions. They did not physically act upon any raw materials and did not constitute part of the manufacturing process. The State Tax Commission found that the computers were not used in manufacturing and, therefore, did not qualify for the investment tax credit.

Since the Legislature knowingly omitted an *investment advisor* from the statutory language of section 210.12(b)(i)(D) by revising the language of 1998 NY Senate Bill S.6248, it limited the qualifying use of property for investment advisory services to the provision of such investment advisory services for a regulated investment company as provided in section 210.12(b)(i)(E) of the Tax Law. This position is supported by the Legislature's stated intent to extend the investment tax credit to the financial services and banking industry for investments in tangible property *similar to the investments that now qualify for manufacturers*, and the denial by the Tax Commission of the investment tax credit for computers used by manufacturers to aid in making management decisions under *Epic Chemicals, supra*. Therefore, investment advisory services provided by a broker or dealer, other than such services provided for a regulated investment company, are not deemed connected with the purchase or sale of securities or commodities and do not constitute a qualifying use of tangible property for purposes of section 210.12(b)(i)(D) and (E) of the Tax Law.

Corporation X states that substantially all of the nonadministrative staff of Corporation X's six business units at issue are licensed as *Series 7 – General Securities Representatives*, which is regulated by NASD. Corporation X also states that many of the administrative employees working within the business units at issue have chosen to obtain their individual *Series 7* license as well. The NASD requirement that any person who is associated with a securities firm and is engaged in the securities business of the firm must register with NASD and have a *Series 7* license does not indicate that the functions these individuals perform are connected with the purchase or sale of securities or commodities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law. For purposes of section 210.12(b)(i) of the Tax Law, all employees of a broker or dealer other than the brokers or dealers engaged in activities in connection with the purchase or sale of securities or commodities pursuant to section 210.12(b)(i)(D) and (E) of the Tax Law are employees performing administrative and support functions that result from or are related to the qualifying use of tangible property, but such administrative employees are not engaged in activities connected with the purchase or sale of securities. (See TSB-M-98(8)C and (6)I, *supra*.)

With respect to the determination of whether, for taxable years 1999, 2000, and 2001, Corporation X's six business units at issue meet the requirements of section 210.12(b)(i)(D) and (E) of the Tax Law, this NYT-G will address each business unit separately.

Investment Banking

This division engages in both underwriting securities as well as the financial advisory services that support those underwriting activities.

(a) The activities of engaging in equity financings in which Corporation X assumes the risk of buying common stock or convertible bonds from an issuing corporation or government entity and reselling them to the investing public either directly or through other dealers, earning a profit on the spread, are activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

(b) The participation in an underwriting syndicate, either as the manager of such syndicate or as a nonmanaging member that simply purchases blocks of the underwritten securities at a discount and resells them to the investing public, is an activity in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

(c) The underwriting of issuances of investment grade securities, including bonds, preferred stock, and derivatives, earning a spread equal to the difference between the price Corporation X pays and the offering price at which Corporation X's resale is made to the public, is an activity in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

(d) The activities of securitizing commercial mortgage debt (by bundling and securitizing the value of outstanding loans), so that those securities can be sold to customers, and monetizing assets (by, for example, creating equity derivatives that can themselves be traded), are activities in connection with the purchase or sale of securities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law. Note that any activities related to mortgage debt origination are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

(e) The activities of engaging in leveraged financing transactions, such as underwriting junk bonds, syndicating loans, or providing derivative financing through which a client might hedge an outstanding securities issuance, with the offsetting instrument then being marketable to the public, are activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

(f) The activities of providing related financial advisory services to help plan for the underlying transaction that creates the client's stock or debt capital needs such as a merger, acquisition, divestiture or some other restructuring, are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

Client Financial Services

This segment counsels individual investors on making new investments or changes in their portfolios and engages in authorized trading, including some discretionary trading, on behalf of customers based on their investment objectives.

(a) The activities of providing investment advisory services for clients are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

(b) The activities of executing sales on behalf of clients in the equities and fixed income markets, including but not limited to purchases and sales of investment funds, whether on a discretionary basis for a fee or nondiscretionary basis for a commission, are activities in

connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

Electronic Trading

The Electronic Trading business unit was established to build a world-class trading system for Corporation X's clients. In developing the Electronic Trading business, Corporation X invested in Web site development, operations and back office systems, investor service center technology, and workplace equipment, primarily purchasing computers and data communications equipment to conduct the Electronic Trading business. Electronic Trading had its own management, technology, finance, marketing, compliance, and products groups.

(a) The activities of the Services group of building the on-line trading system capability of Electronic Trading and enabling the trading of securities are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law (hereinafter, for Electronic Trading, the phrase "not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law" is referred to as "nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law."

(b) The activities of the Order group of building the back-end supporting systems by which Electronic Trading orders were handled are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(c) The activities of the Client Financial Services group of building the call center software used by employees outside New York State are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(d) The activities of the Data Architecture group of creating the database and access to data sources are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(e) The activities of the Operations/Finance group of building the on-line account opening system are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(f) The activities of the Content group of controlling the data sources available on the Electronic Trading platform are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(g) The activities of the Client Financial Services Site group of handling how investor portfolios would be displayed on the Electronic Trading Web site are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(h) The activities of the Multi services group of consulting with all other products groups are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(i) The activities of the Production support team of working with the technology development team to develop systems that would enable 24/7 support of the Electronic Trading Web site are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(j) The activities of the Market data infrastructure team are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(k) The activities of the Networking infrastructure group of being responsible for the networking infrastructure and Internet connectivity functions, and being involved in the original hardware purchases are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(l) The activities of Quality Assurance of testing systems before they went to the production stage are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(m) The activities of the Products business unit of defining what was built into the Electronic Trading platform, writing product specifications, ensuring that other groups met the standards they had designated, designing the Web site, defining how the Web site should look and its functionality, and interfacing with other teams are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(n) The activities of the Sales business unit of handling all marketing functions are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(o) The activities of the Finance group of doing all of the financial projections for Electronic Trading, keeping track of sales and fixed and variable costs in all the other departments, and tracking costs spent on technology, marketing, and operations are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

(p) The facts presented by Corporation X do not make clear the nature of the activities conducted by Electronic Trading employee representatives on the trading desk. However, assuming these are Electronic Trading employees and the activities conducted by such employees are the trading of securities, such activities are activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

(q) The activities of Electronic Trading employees dedicated to management functions and legal and business support services are nonqualifying activities pursuant to sections 210.12(b)(i)(D) and (E) of the Tax Law.

It should be noted that the Electronic Trading business unit became operational in 2000 and 2001. Once the Electronic Trading unit became engaged in activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law, equipment used in connection with such activities could qualify for the investment tax credit pursuant to sections 210.12(b)(i)(D) and (E).

Prime Brokerage

This segment acts as the prime broker for various hedge fund clients. Through Corporation X, customers are provided securities lending services that give them access to hard-to-borrow securities.

(a) The broker activities and the activities of compiling lists of trades and reporting the daily transactions of the hedge fund and monitoring the risks of the hedge fund and its margin loan borrowings are activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law. However, the activity of providing information to assist investment managers and hedge funds in making purchase and sale decisions are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

(b) It is not clear from the facts whether the activities of developing and implementing key technologies to speed execution and increase the flow of information are conducted by employees of the Prime Brokerage segment. In any event, these activities are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan

arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

Operations

This division provides integrated and highly secure operations services to several business units within Corporation X.

(a) The activities of processing, clearing, and settling trades in a timely and accurate manner in connection with the purchase or sale of securities by business units within Corporation X are activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

(b) The activities of managing the reconciliation and payment processes both internally between Corporation X departments and externally between Corporation X and banks and exchanges in connection with the purchase or sale of securities by business units within Corporation X are activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law. The activities of managing the flow of information, including account management and investment performance measurement, that are essential for the Investment Management Division to plan and implement securities trades for its clients are activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law.

(c) To the extent that the activities of supporting various business products for Corporation X's Equities Division and many other products go beyond the support activities described above, they may be back office functions that are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

(d) To the extent that the activities of supporting several products for Corporation X's Fixed Income division go beyond the support activities described above, they may be back office functions that are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

Research

This department performs a differentiated research effort that is firmly aligned with the interests of Corporation X's investing clients as an important part of its Equities business. The activities of engaging in global research to provide industry expertise, independent thinking, and timely insights to investors are not activities in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(D) of the Tax Law, or activities in the provision of investment advisory services for a regulated investment company (as defined in IRC section 851) or activities in connection with lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities pursuant to section 210.12(b)(i)(E) of the Tax Law.

Conclusion

Tangible property that meets the principal use requirements of sections 210.12(b)(i)(D) and (E) of the Tax Law in the qualifying activities described above may qualify for the investment tax credit, if the property meets the other requirements of section 210.12(b)(i) of the Tax Law and if all or a substantial portion of the taxpayer's employees performing the administrative and support functions resulting from or related to the qualifying uses of the property are located in New York State.

However, whether the property purchased by Corporation X actually qualifies for the investment tax credit is a question of fact not susceptible of determination in a NYT-G. The necessary factual determination would have to be made within the context of an audit in accordance with the principles outlined above.

NOTE: An NYT-G is an informational statement of the Department's interpretation of the law, regulations, and Department policies and is usually based on a particular set of facts or circumstances. It is accurate on the date issued and is limited to the facts set forth therein. NYT-Gs are published to provide information and guidance to taxpayers, Department personnel, and tax professionals. Subsequent changes in the law or regulations, judicial decisions, Tax Appeals Tribunal decisions, or changes in Department policies could affect the validity of the information presented in an NYT-G.