

NEW JERSEY TAX
ALERT

OCTOBER
2006

OUT-OF-STATE LICENSER MUST PAY N.J. CORPORATION BUSINESS TAX

Corporations with no physical presence in New Jersey (other than their trademark) are now subject to New Jersey's Corporation Business Tax, *N.J.S.A.* 54:10A-1 to -41. The Supreme Court of New Jersey ruled in favor of the State in *Lanco, Inc. v. Director, Division of Taxation* in its October 12, 2006 opinion. The Court affirmed an Appellate Division decision that New Jersey may subject a foreign corporation to the Corporation Business Tax even though the corporation has no physical presence in New Jersey. The Court based its decision upon the fact that Lanco derives its income from a New Jersey source pursuant to a license agreement for the use of its trademark by another corporation that conducts retail business in New Jersey.

Lanco, incorporated in Delaware, is a Delaware investment holding company that licenses its intellectual property (e.g. trademarks) to its parent corporation, clothing retailer Lane Bryant. While Lanco has no physical presence in New Jersey, it earns money in New Jersey, which the Court held subjects it to taxation upon that income.

The U.S. Supreme Court has already determined that, at least for sales and use taxes, a corporation must have

a physical presence in the state in order to establish the constitutionally required "substantial nexus." See *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). Since the Court's decision in *Quill*, many courts throughout the country have been asked to review the question of whether *Quill* is limited to sales and use taxes or whether it also applies to income/franchise taxes. The result has been that a split of authority has developed among various state courts that have addressed this question. The N.J. Supreme Court found that *Quill* is indeed limited to sales and use taxes.

Because this ruling raises a constitutional question under the Commerce Clause as to whether such a foreign corporation must have a physical presence for state income taxation, Lanco may file a petition for certiorari with the U.S. Supreme Court.

If you have any questions concerning the N.J. Supreme Court's *Lanco* decision or, in general, the operation of and benefits that might be derived from a Delaware investment holding company, Schnader Harrison Segal & Lewis LLP lawyers can guide you through the "traps for the unwary."

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