

**New York State Department of Taxation and Finance**  
**Office of Tax Policy Analysis**  
**Technical Services Division**

TSB-A-02(10)C  
Corporation Tax  
June 26, 2002

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C011011A

On October 11, 2001, a Petition for Advisory Opinion was received from Deloitte & Touche LLP, Attn. Russell W. Banigan, 1633 Broadway, New York, New York 10019-6754.

The issue raised by Petitioner, Deloitte & Touche LLP, is whether interest income from items of “cash”, other than cash on deposit with a bank, may be allocated by a zero investment allocation percentage under section 210.3(b) of the Tax Law, where the taxpayer is eligible to treat its cash on hand and on deposit as investment capital under section 208.7(a) of the Tax Law.

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

XYZ corporation owns money market mutual funds and various U.S. Treasury Notes and Treasury Bills, and is not a dealer in securities. The U.S. Treasury Notes and Treasury Bills are purchased as part of XYZ’s laddered cash management program and their maturity dates generally range from three months to four years from the date of purchase. In addition, XYZ has money on deposit in various interest bearing bank accounts, which are payable upon demand.

At any given point in time, XYZ’s portfolio consists of both short-term investments (items payable on demand or that are within six months and one day of maturity) and non-short-term investments (items that are more than six months and one day from maturity). The short-term investments include interest bearing bank accounts, money market mutual funds and U.S. Treasury Notes and Treasury Bills maturing within six months and one day. The non-short-term investments consist of U.S. Treasury Notes that are not within six months and one day of maturity (“above the line” investment capital). These “above the line” U.S. Treasury Notes generally constitute at least 40 percent of XYZ’s investment capital (for this purpose, investments in the mutual funds, U.S. Treasury Bills and Treasury Notes and various bank deposits are counted as investment capital). XYZ owns no other items of investment capital.

On its tax return for the current year, XYZ elects to treat its items of “cash” as investment capital. Since its only items of “above the line” investment capital are U.S. obligations with a zero issuer’s allocation percentage, XYZ’s investment allocation percentage for the current year is zero. XYZ’s New York business allocation percentage is greater than zero.

**Law and Regulations**

Section 208.7(a) of the Tax Law provides that the term “business capital” means “all assets, other than subsidiary capital, investment capital and stock issued by the taxpayer, less liabilities not

deducted from subsidiary or investment capital except that cash on hand and on deposit shall be treated as investment capital or as business capital as the taxpayer may elect.”

Section 208.5 of the Tax Law provides that the term “investment capital” means “investments in stocks, bonds and other securities, corporate and governmental, not held for sale to customers in the regular course of business, exclusive of subsidiary capital and stock issued by the taxpayer, provided, however, that, in the discretion of the commissioner, there shall be deducted from investment capital any liabilities which are directly or indirectly attributable to investment capital ....”

Section 3-3.2(a)(1) of the Business Corporation Franchise Tax Regulations (“Article 9-A Regulations”) provides, in pertinent part, that:

The term “investment capital” means the taxpayer’s investments in stocks, bonds and other securities issued by a corporation (except as provided in paragraph (2) of this subdivision) or by the United States, any state, territory or possession of the United States, the District of Columbia, or any foreign country, or any political subdivision or governmental instrumentality of any of the foregoing . . . . At the election of the taxpayer, cash on hand and cash on deposit may be treated on any report as either investment capital or business capital . . . . Any debt instrument, including a certificate of deposit, which is described in paragraph (2) or (3) of subdivision (c) of this section and is not described in paragraph (2) of this subdivision and which is payable by its terms on demand or within six months and one day from the date on which the debt was incurred is deemed to be cash on hand or on deposit. Any such debt instrument which is payable by its terms more than six months and one day from the date on which the debt was incurred is deemed to be cash on hand or on deposit on any day which is not more than six months and one day prior to its date of maturity. Cash also includes shares in a money market mutual fund. A money market mutual fund is a no-load, open-end investment company registered under the Federal Investment Company Act of 1940 which attempts to maintain a constant net asset value per share and holds itself out to be a “money market” fund. A taxpayer may not elect to treat part of its cash as investment capital and part as business capital. No election to treat cash as investment capital may be made where the taxpayer has no other investment capital.

Section 3-3.2(a)(2) of the Article 9-A Regulations provides that:

Investment capital does not include:

- (i) stock issued by the taxpayer;
- (ii) stocks, bonds or other securities constituting subsidiary capital;

(iii) securities of an individual, partnership, trust or other nongovernmental entity which is not a corporation within the definition contained in section 208.1 of the Tax Law (such as [FNMA and GNMA] pass-through certificates);

(iv) stocks, bonds and other securities of a DISC, or any indebtedness from a DISC;

(v) regular interests and residual interests in a real estate mortgage investment conduit (REMIC), as defined in section 860D of the Internal Revenue Code;

(vi) futures contracts and forward contracts; and

(vii) stocks, bonds and other securities held by the taxpayer for sale to customers in the regular course of its business.

Section 3-3.2(c) of the Article 9-A Regulations provides that:

For purposes of paragraph (1) of subdivision (a) of this section, the phrase “stocks, bonds and other securities” means:

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(2) debt instruments issued by the United States, any state, territory or possession of the United States, the District of Columbia, or any foreign country, or any political subdivision or governmental instrumentality of any of the foregoing;

(3) qualifying corporate debt instruments (see subdivision (d) of this section) . . . .

Section 3-3.2(d)(1) of the Article 9-A Regulations provides that:

The term “qualifying corporate debt instruments” means all debt instruments issued by a corporation other than the following:

(i) instruments issued by the taxpayer or a DISC;

(ii) instruments which constitute subsidiary capital in the hands of the taxpayer;

(iii) instruments acquired by the taxpayer for services rendered or for the sale, rental or other transfer of property, where the obligor is the recipient of the services or property; however, where a taxpayer sells or otherwise transfers property which

is investment capital in the hands of such taxpayer (e.g., stock) and receives in return a corporate obligation issued by the recipient of such property, such corporate obligation, if it is not otherwise excluded from the category of investment capital, would constitute investment capital in the hands of the taxpayer;

(iv) instruments acquired for funds if:

(a) the obligor is the recipient of such funds;

(b) the taxpayer is principally engaged in the business of lending funds; and

(c) the obligation is acquired in the regular course of the taxpayer's business of lending funds;

(v) accepted drafts (such as banker's acceptances and trade acceptances) where the taxpayer is the drawer of the draft;

(vi) instruments issued by a corporation which is a member of an affiliated group which includes the taxpayer; and

(vii) accounts receivable, including those held by a factor.

Section 208.6 of the Tax Law provides that the term "investment income" means "income, including capital gains in excess of capital losses, from investment capital, to the extent included in computing entire net income, less, (a) in the discretion of the commissioner, any deductions allowable in computing entire net income which are directly or indirectly attributable to investment capital or investment income . . . ."

Section 210.3(b) of the Tax Law provides that a taxpayer "[multiplies] its investment income by an investment allocation percentage . . . ." Section 210.3(b)(3) of the Tax Law provides, in pertinent part, that "if a taxpayer's investment allocation percentage is zero, interest received on bank accounts shall be multiplied by its business allocation percentage."

### **Discussion**

"Cash on hand and cash on deposit" as used in section 208.7(a) of the Tax Law is not defined in Article 9-A of the Tax Law or in the Article 9-A Regulations. However, section 3-3.2(a)(1) of the Article 9-A Regulations, in defining investment capital, provides that any debt instrument, including a certificate of deposit, which is described in section 3-3.2(c)(2) or (3) of the Article 9-A Regulations, and is not described in section 3-3.2(a)(2) of the Article 9-A Regulations, and which is payable by its terms on demand or within six months and one day from the date on which the debt

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was incurred is deemed to be cash on hand or on deposit. Any such debt instrument which is payable by its terms more than six months and one day from the date on which the debt was incurred is deemed to be cash on hand or on deposit on any day which is not more than six months and one day prior to its date of maturity.

In this case, XYZ has investments throughout the year in U.S. Treasury Notes not maturing within six months and one day that constitute investment capital pursuant to section 3-3.2(c)(2) of the Article 9-A Regulations. XYZ also has investments in interest bearing bank accounts, money market mutual funds and U.S. Treasury Notes and Treasury Bills maturing within six months and one day, thereby constituting cash on hand and cash on deposit as used in section 208.7(a) of the Tax Law and section 3-3.2(a)(1) of the Article 9-A Regulations. Since XYZ has items of investment capital, namely, the U.S. Treasury Notes not maturing within six months and one day, XYZ is allowed, pursuant to section 3-3.2(a)(1) of the Article 9-A Regulations, to elect to treat the investments constituting cash as investment capital.

Income from XYZ's investment capital (the U.S. Treasury Notes not maturing within six months and one day) and, since XYZ has elected, all of XYZ's items of cash on hand and on deposit (the investments in interest bearing bank accounts, money market mutual funds and U.S. Treasury Notes and Treasury Bills maturing within six months and one day) constitute investment income pursuant to section 208.6 of the Tax Law.

Pursuant to section 210.3(b) of the Tax Law, XYZ's investment income is multiplied by its investment allocation percentage. However, since XYZ's investment allocation percentage is zero, section 210.3(b)(3) of the Tax Law provides that XYZ's investment income that represents interest income received on bank accounts must be multiplied by XYZ's business allocation percentage. XYZ's investment income attributable to XYZ's items of cash on hand and on deposit, other than interest received on bank accounts, is multiplied by XYZ's zero investment allocation percentage.

DATED: June 26, 2002

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