

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-82(12)C
Corporation Tax
August 25, 1982

STATE OF NEW YORK
STATE TAX COMMISSION

ADVISORY OPINION

PETITION NO. C810810A

On August 10, 1981 a Petition for Advisory Opinion was received from The Chase Manhattan Bank, N.A., One Chase Manhattan Plaza, New York, N.Y. 10081.

Petitioner has framed its request for an Advisory Opinion in the form of a number of requests for rulings. Each of these consists of a request that the Tax Commission adopt a specified position with respect to international banking facilities (hereinafter referred to as "IBFs"). In what follows, the ruling requests will be set forth in the form and order presented by Petitioner, and the appropriate responses will follow each request. A "yes" response indicates the adoption of the proposed ruling, with whatever modifications are there stated. A "no" response indicates a declination to adopt the proposed ruling. The responses to Petitioner's ruling requests are based largely on recently promulgated Regulations of the State Tax Commission regarding international banking facilities, and citations to supporting or elucidating provisions of such Regulations are made wherever appropriate.

I. ELIGIBLE GROSS INCOME

Rulings Requested

a. Documenting income on loans to foreign persons

Ruling Requested - We request that you rule that the amounts of IBF loans and IBF deposits shall be determined by reference to the taxpayer's reports to the Federal Reserve Board.

Response- No. See 20 NYCRR 38.4.

b. Documenting use of proceeds

Ruling Requested - We request that you rule that the use of proceeds requirement of the Tax Law be deemed satisfied where the IBF provided the borrower with the required notice, and received any required written acknowledgment of such notice, pursuant to Federal Reserve Board Reg. Sec. 204.8(b).

Response- No. In addition to the factors cited by Petitioner, the IBF must also obtain and retain a borrower's statement of the purpose of the loan. See 20 NYCRR 38.4(b).

c. Other eligible gross income

Rulings Requested - We request that you rule that:

(1) the eligible gross income of an IBF includes related foreign exchange trading or hedging transactions even though the transactions are not recorded in the financial accounts of the IBF.

Response- No. See 20 NYCRR 38.4(d).

(2) the eligible gross income of an IBF also includes the income arising from other IBF transactions and activities permissible under the Tax Law even though the related transactions, assets and liabilities are not recorded in the financial accounts of the IBF.

Response- No. See 20 NYCRR 38.1(c)(3) and 20 NYCRR 38.4(a).

(3) the term "related foreign exchange trading or hedging transaction" means:

(i) The purchase, sale or exchange of foreign currency in connection with the receipt or disbursement of funds in an IBF loan or deposit placement transaction or with respect to a deposit in an IBF (IBF borrowing); or

(ii) The acquisition, disposition or performance of any contract to purchase, sell or exchange foreign currency at a future date under terms fixed in the contract if the contract hedges a foreign currency-denominated IBF loan, IBF deposit or IBF borrowing. A forward contract hedges a foreign currency-denominated IBF loan, IBF deposit or IBF borrowing if the effect of a change in the value of the foreign currency on the United States dollar value of the forward contract, either alone or in combination with other such contracts, offsets the effect of the change on the United States dollar value of the foreign-currency-denominated IBF loan, IBF deposit or IBF borrowing. A hedging relationship may be established either by reference to particular facts and circumstances (e.g., the amount of the forward contract, particular currency, initial date and maturity) indicating a hedging purpose, or by designating a contract as being intended for the purpose of hedging an IBF loan, IBF deposit or IBF borrowing.

Response- No. See 20 NYCRR 38.4(d).

II. APPLICABLE EXPENSES

Rulings Requested

a. Interest expense

Rulings Requested - It is requested that you rule that:

(1) the IBF shall bear the appropriate amount of interest expense associated with each borrowing which is recorded in the financial accounts of the IBF. For this purpose, the term "borrowing" includes a deposit or placement which is represented by a promissory note,

acknowledgment of advance, or similar obligation (written or oral) which is issued as a means of obtaining funds for the IBF.

Response- No. For appropriate amount of interest expense associated with each borrowing, see 20 NYCRR 38.6. Borrowing is included in the definition of "deposit". See 20 NYCRR 38.2(c).

(2) the interest expense appropriate to an IBF borrowing from an unrelated party shall be the amount of interest paid to the unrelated party, or accrued with respect to that borrowing in accordance with the IBF accounting method and subsequently paid.

Response- Yes, to the extent that the interest expense is included in the computation of entire net income and 26 CFR 1.882-5 is not used for Federal income tax purposes. See 20 NYCRR 38.6.

(3) the interest expense appropriate to an IBF borrowing from a related corporate entity shall be the open market rate of interest appropriate to a borrowing of that type.

Response- No. See 20 NYCRR 38.6.

(4) the interest expense appropriate to an IBF borrowing from another office of the taxpayer shall be based on the average interest rate incurred by the lending office which shall be equal to the ratio of the total amount of interest expense recorded in the financial accounts of the lending office to the average total amount of assets recorded in the financial accounts of the lending office. This computation shall be made on a daily, monthly, quarterly or annual basis, at the taxpayer's option, but once made shall be consistently applied.

Response- No. See 20 NYCRR 38.6.

b. Bad Debt Deduction

Rulings Requested - It is requested that you rule that:

(1) the amount of the bad debt deduction that is allocable to the IBF may be determined by reference to the bad debt deduction claimed by the taxpayer in its New York State franchise with respect to loans and charge-offs of the IBF.

Response- No. See 20 NYCRR 38.7

(2) the taxpayer may transfer to the IBF the amount of the reserve for bad debts maintained by the taxpayer in accordance with the Tax Law with respect to loans transferred to the IBF, as of the date of transfer of such loans. Such transfer shall not result in the realization of taxable income or deductible expense to either the taxpayer or the IBF.

Response- Yes.

c. Other Deductions

Rulings Requested - It is requested that you rule that:

(1) each other deduction (other than interest expense and the bad debt deduction) of the taxpayer that is directly related on the basis of facts and circumstances to the income, gains, deductions, assets or liabilities of the IBF, i.e., (i) incurred as a result of, or incident to, an activity from which such income, gains, deductions, assets or liabilities arise, or (ii) incurred in connection with such assets or liabilities, shall be treated as an expense attributable to the IBF.

Response- Yes. See 20 NYCRR 38.5 and 20 NYCRR 38.9.

(2) the taxpayer shall apportion among an IBF and the places of business of the taxpayer located within and without New York State (treating the IBF for this purpose as a place of business of the taxpayer located outside New York State) each other deduction that is not directly related to the income, gains, deductions, assets or liabilities of the IBF on the basis of the factual relationship between the deduction and the income, gains, deductions, assets or liabilities of the IBF. Such deductions may be apportioned to the IBF in the ratio of the average aggregate amount for the taxable year of the assets of the IBF to the average aggregate amount for the taxable year of all the assets of the taxpayer.

Response- No. See 20 NYCRR 38.8 and 20 NYCRR 38.9.

d [c]. Allocation to eligible gross income

Rulings Requested - It is requested that you rule that:

(1) the bad debt deduction and other deductions attributable to the IBF be directly reduced where those attributable expenses are directly related to the IBF's ineligible gross income or the loans giving rise to that ineligible gross income, and

Response- Yes. See 20 NYCRR 38.9.

(2) the balance of such attributable expenses and the interest expense attributable to the IBF be allocated between the IBF's ineligible and eligible gross income based on the ratio of the loan balances (computed daily, monthly, quarterly or annually at the taxpayer's option and consistently applied) with respect to the loans giving rise to ineligible and eligible gross income and that the expenses so attributable to the IBF be reduced by the amount so allocated to ineligible gross income.

Response- No. See 20 NYCRR 38.9.

III. INELIGIBLE FUNDING AMOUNT

Rulings Requested

a. IBF balance sheet items

Rulings Requested - It is requested that you rule that:

(1) accrued interest, taxes and other current expenses, accounts payable, reserves for deferred taxes and loan losses, and retained earnings may be treated as IBF liabilities whether or not they are reflected in the accounts of the IBF or are indirectly reflected through some mechanism allowable under the Federal Reserve Board rules.

Response- No. See 20 NYCRR 38.1(c) and 38.10(b).

(2) accrued interest, taxes and other current expenses, accounts payable, and reserves for deferred taxes and loan losses shall be eliminated from both the numerator and denominator of the ineligible funding fraction.

Response- No. See 20 NYCRR 38.10.

(3) retained earnings of an IBF are treated as lendable funds received from foreign persons.

Response- No. See 20 NYCRR 38.10(c).

(4) an IBF deposit includes a borrowing, deposit or placement which is represented by a promissory note, acknowledgment of advance, or similar obligation (written or oral) which is recorded in the financial accounts of an IBF and which is issued, as a means of obtaining funds for the IBF, to one or more foreign persons.

Response- No. See 20 NYCRR 38.2(c).

(5) the "average aggregate amount" of liabilities and other sources of funds generally is to be computed on a quarterly or more frequent basis, at the option of the taxpayer, provided that the computations are made on a consistent basis.

Response- Yes. See 20 NYCRR 38.10(b).

b. Intercompany deposits from U.S. offices

Ruling Requested - It is requested that you rule that:

(1) there shall be excluded from the numerator and the denominator of the fraction described in Section 1453(f)(5) of the Tax Law an amount determined by multiplying the average aggregate amount for the taxable year of all liabilities and other sources of funds of the IBF by a fraction:

(A) the numerator of which is the average aggregate amount for the taxable year of the loans and deposits of the IBF which were ineligible IBF loans or IBF deposit placements, and

(B) the denominator of which is the average aggregate amount for the taxable year of all the loans and deposit placements of the IBF.

Response- No. The statutory formula arrives at an appropriate result because the ineligible funding fraction is applied only to eligible net income, not total net income.

IV. FLOOR AMOUNT

Rulings Requested

a. Developing Information

Rulings Requested - It is requested that you rule that:

(1) the floor amount for an IBF for the taxable year is computed by taking into account only the loans made to, and deposits placed with, foreign persons by the taxpayer. In the case of a taxpayer which, pursuant to Section 1462(f) of the Tax Law, made a consolidated return with corporations affiliated with it for any of the taxable years 1975, 1976 and 1977, or makes a consolidated return for the taxable year, the taxpayer shall compute the floor amount as if it had filed separate returns for the taxable years 1975, 1976 and 1977 and as if it were filing a separate return for the taxable year.

Response- Yes. See 20 NYCRR 38.11(c).

(2) the amounts of the taxpayer's loans to foreign persons and deposits with foreign persons which are banks (including subsidiaries of the taxpayer) or foreign branches of banks (including foreign branches of the taxpayer), which loans and deposits were recorded in the financial accounts of the taxpayer for its branches, agencies and offices within New York State for the taxable years 1975, 1976 and 1977, may be determined by reference to the monthly or quarterly reports of the taxpayer to the Federal Reserve Bank of New York. The amount of such loans or deposits shall not be reduced, increased, or offset by any other balances to or from such persons which do not appear as loans or deposits in such reports.

Response- No. Appropriate modifications must be made to the figures contained in the taxpayer's report to the Federal Reserve Bank of New York. See 20 NYCRR 38.11(a)(1)(i).

(3) the average aggregate amount of loans made to, and deposits placed with, foreign persons by the taxpayer for any taxable year generally is to be computed on a quarterly basis, or, at the taxpayer's option, on a more frequent basis. The computation shall be made on a consistent basis for all taxable years.

Response- Yes. See 20 NYCRR 38.11(b).

b. Treatment of ineligible loans

Ruling Requested - It is requested that you rule that IBF loans, which in effect do not give rise to eligible gross income by virtue of being ineligible funded, be treated as loans of the taxpayer (other than the IBF) for purposes of computing the floor amount.

Response- No. The funding of an IBF loan has no bearing on whether the loan produces eligible gross income. Accordingly, such income must be included in the computation of the floor amount.

V. ESTABLISHMENT OF AN IBF

Rulings Requested

a. NYS qualification and definitions

Rulings Requested - It is requested that you rule that:

(1) an IBF shall be deemed established when the requisited requirement for establishment of an IBF under the FRB regulations are complied with; that is, an accounting segregation has been made and the 14 days notice has been provided.

Response- No. See 20 NYCRR 38.1(c).

(2) the term "international banking facility" or "IBF" shall have the meaning set forth in the regulations of the Board of Governors of the Federal Reserve System and official interpretations thereof.

Response- No. The applicable definition is that set forth in Tax Law, § 1450(c).

b. Year of transfer

Rulings Requested - It is requested that you rule that:

(1)(a) the tax year of the IBF shall end at the same time as that of the taxpayer and
(b) any resulting short year of the IBF shall be treated as a full year for all purposes, including the floor amount computations.

Response- (a) Yes.
(b) No. In the case of a short taxable year, all liabilities and assets must be pro-rated. A short taxable year is treated as a full taxable year for purposes of the percentage amounts set forth in 20 NYCRR 38.11(a)(ii).

(2) no gain or loss shall be recognized to the taxpayer upon the transfer by the taxpayer to the IBF of assets and liabilities and the IBF shall have the same tax bases as that of the taxpayer.

Response - Yes.

DATED: August 20, 1982

s/LOUIS ETLINGER
Deputy Director
Technical Services Bureau