

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

TSB-A-83(8)C
Corporation Tax
May 9, 1984

STATE OF NEW YORK
STATE TAX COMMISSION

ADVISORY OPINION

PETITION NO. C820629A

On June 29, 1982 a Petition for Advisory Opinion was received from Chase Manhattan Bank, N.A., 1 Chase Manhattan Plaza, New York, New York 10081.

Petitioner inquires as to whether two new corporations, first and second tier subsidiaries, respectively, of Chase Manhattan Capital Markets (Holdings), Inc. (hereinafter "CMCMHI"), will be permitted to file franchise tax reports under Article 9-A of the Tax Law on a combined basis. Petitioner also inquires as to whether certain interest payments made by such new corporations would be subject to the interest add-back requirement set forth in section 208.9(b)(5) of the Tax Law. The two new corporations referred to are Chase Manhattan Capital Markets Corporation (hereinafter "CMCM"), a subsidiary of CMCMHI, which is itself a subsidiary of Chase Manhattan Bank, N.A. (hereinafter "CMB"), and Chase Manhattan Government Securities, Inc. (hereinafter "CMGS"), a subsidiary of CMCM.

Petitioner has provided the following statement of facts as a basis for the requested Advisory Opinion. CMCM will be a registered securities dealer with the Securities and Exchange Commission and the National Association of Securities Dealers. In addition, it will conduct domestic merchant banking activities, such as acting as a financial advisor in connection with acquisitions and mergers and arranging loan syndications and placements. CMCM will have offices in New York. CMGS will be a non-registered government securities dealer trading in U.S. government and Federal agency obligations. Its office will be in New York.

CMCM, as a registered securities dealer, will trade, underwrite and sell municipal securities for customers and for its own account. The company will also provide certain services to states and municipalities such as advising on how to manage finances and arranging financing, including loan syndications and the underwriting of securities. In addition, it will provide certain financial advisory services including those related to private placements and mergers and acquisitions and loan syndications. CMCM will also be positioned to underwrite revenue bonds and conduct money market fund operations if proposed legislation authorizing such activities is enacted.

CMGS will be formed as a separate legal entity, and will not be required to register with any federal securities regulatory body so long as it engages only in activities in U.S. Treasury and Federal Agency securities, such as buying and selling such securities for customers and for its own account. Because CMGS will not be a federally registered securities dealer, its sales personnel cannot take any order for other types of securities, including without limitation municipal securities or other obligations, and all inquiries for such securities will be referred to CMCM. When CMCM salesmen

receive an inquiry regarding U.S. Treasury or Federal Agency securities, any resulting order would be executed as agent for CMGS. It is also expected that CMCM will provide certain administrative services (e.g., accounting, purchasing, etc.) and operational assistance to CMGS, that certain executive officers of CMCM will also act in that capacity for CMGS, and that CMCM will exercise fiscal and management control over CMGS.

While it is contemplated that the proposed capitalization of the two companies will fully support their respective securities activities, it is possible that short-term borrowings from CMB may be required from time to time to allow them to carry their inventories of securities.

Section 211.4 of the Tax Law provides for the filing of franchise tax returns on a combined basis, as follows:

"In the discretion of the tax commission, any taxpayer, which owns or controls either directly or indirectly substantially all the capital stock of one or more other corporations, or substantially all the capital stock of which is owned or controlled either directly or indirectly by one or more other corporations or by interests which own or control either directly or indirectly substantially all the capital stock of one or more other corporations, may be required or permitted to make a report on a combined basis covering any such other corporations and setting forth such information as the tax commission may require . . . "

Sections 6-2.1 et seq of the Franchise Tax Regulations set forth the requirements which must be met before the Tax Commission will exercise its discretion in requiring or permitting the filing of reports on a combined basis.

The first such requirement, that of sufficient stock ownership or control, is clearly met here, inasmuch as CMGS is estated to be a wholly owned subsidiary of CMGS.

The second requirement is that "the corporations are in substance parts of a unitary business conducted by the entire group of corporations . . ."20 NYCRR 6-2.3(a)(1). This requirement is met where, as here, the corporations in question are "engaged in the same or related lines of business . . ."20 NYCRR 6-2.3(b).

The third requirement is that there be "substantial intercorporate transactions among the corporations."20 NYCRR 6-2.3(a)(2). This requirement is met where 50 per cent or more of a corporation's receipts are from activities related to the activities of the other corporation or corporations in a proposed group. Such qualified activities include manufacturing or acquiring goods or property for other corporations in the group, selling goods acquired from other corporations in the group, or financing sales of other corporations in the group. The facts set forth by Petitioner do not indicate the existence of such substantial intercorporate transactions.

Accordingly, under the facts presented, CMCM and CMGS would not be permitted to file their franchise tax reports on a combined basis.

II

The second issue raised by Petitioner relates to the deductibility of interest paid by CMCM and CMGS on loans from CMB.

Section 208.9(b)(5) of the Tax Law provides for the disallowance of certain amounts of interest paid on "indebtedness directly or indirectly owed to any stockholder or shareholder (including subsidiaries of a corporate stockholder or shareholder), . . . owning in the aggregate in excess of five per centum of the issued capital stock of the taxpayer "

In the present instance the interest paid by CMCM to CMB would be interest paid on indebtedness not to a shareholder but to a grandparent. Accordingly the disallowance provided for by section 208.9(b)(5) of the Tax Law would not be applicable. The same conclusion would apply, a fortiori, to interest payments made by CMGS to CMB. The Ore and Chemical Corporation, State Tax Commission Advisory Opinion, TSB-A-82(15)C.

DATED: July 8, 1983

s/FRANK J. PUCCIA
Director
Technical Services Bureau