

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

TSB-A-07(4)I
Income Tax
April 13, 2007

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. I061027A

On October 27, 2006, a Petition for Advisory Opinion was received from Church Communities Inc., c/o David L. Evans, CPA, UHY Advisors NY, Inc., 66 State Street, Albany, New York 12207.

The issue raised by Petitioner, Church Communities Inc., is how to allocate investment tax credits and other economic-based tax incentives among members of a tax-exempt organization recognized under section 501(d) of the Internal Revenue Code (IRC) when that organization engages in business activity in New York State.

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

Petitioner is a religious or apostolic organization recognized under section 501(d) of the IRC (501(d) organization). As a 501(d) organization, Petitioner has a common treasury and engages in business for the common benefit of its individual members. Petitioner's business activity involves manufacturing wood furniture, toys, and mobility equipment for the physically challenged. Petitioner plans to expand its business in New York State.

For federal income tax purposes, Petitioner is required to compute its net income as a corporation and file an annual information return on Form 1065, *U.S. Return of Partnership Income*, to report income of the common treasury. The entire taxable income of Petitioner is allocated to its members and reported as a dividend on each member's federal personal income tax return.

Petitioner's members, all of whom have lifetime vows of personal poverty and obedience, live communally. Members have no private property and are not paid salaries or other remuneration. Collectively and for the common benefit, the members operate a variety of domestic manufacturing businesses. Income earned by an individual member's efforts is pooled into the common treasury, from which goods and provisions are purchased and distributed to members on the basis of need. All members are supported at the same modest standard of living, regardless of their economic contribution to the common treasury.

Applicable law and regulations

Section 501(a) of the IRC provides:

Exemption from taxation. An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

Section 501(d) of the IRC provides:

Religious and apostolic organizations. The following organizations are referred to in subsection (a): Religious or apostolic associations or corporations, if such associations or corporations have a common treasury or community treasury, even if such associations or corporations engage in business for the common benefit of the members, but only if the members thereof include (at the time of filing their returns) in their gross income their entire pro rata shares, whether distributed or not, of the taxable income of the association or corporation for such year. Any amount so included in the gross income of a member shall be treated as a dividend received.

Section 7701(a)(2) of the IRC provides:

Partnership and partner. The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization.

Section 1.501(d)-1(a) of the Treasury Regulations provides:

Religious or apostolic associations or corporations are described in section 501(d) and are exempt from taxation under section 501(a) if they have a common treasury or community treasury, even though they engage in business for the common benefit of the members, provided each of the members includes (at the time of filing his return) in his gross income his entire pro rata share, whether distributed or not, of the net income of the association or corporation for the taxable year of the association or corporation ending with or during his taxable year. Any amount so included in the gross income of a member shall be treated as a dividend received.

Section 1.6033-1(a)(5)(i) of the Treasury Regulations provides:

Every religious or apostolic association or corporation described in section 501(d) which is exempt from taxation under section 501(a) shall file a return on Form 1065 for each taxable year, stating specifically the items of gross income and deductions, and its taxable income. There shall be attached to the return as a part thereof a statement showing the name and address of each member of the association or corporation and the

amount of his distributive share of the taxable income of the association or corporation for such year.

Section 301.6104(d)-1 of the Treasury Regulations provides, in part:

(a) In general. Except as otherwise provided in this section, if a tax-exempt organization (as defined in paragraph (b)(1) of this section) filed an application for recognition of exemption under section 501, it shall make its application for tax exemption (as defined in paragraph (b)(3) of this section) available for public inspection without charge at its principal, regional and district offices during regular business hours. Except as otherwise provided in this section, a tax-exempt organization shall make its annual information returns (as defined in paragraph (b)(4) of this section) available for public inspection without charge in the same offices during regular business hours. . . .

(b) Definitions. For purposes of applying the provisions of section 6104(d), this section and section 301.6104(d)-2 and 301.6104(d)-3, the following definitions apply:

(1) Tax-exempt organization. The term tax-exempt organization means any organization that is described in section 501(c) or section 501(d) and is exempt from taxation under section 501(a). The term tax-exempt organization also includes any nonexempt charitable trust described in section 4947(a)(1) or nonexempt private foundation that is subject to the reporting requirements of section 6033 pursuant to section 6033(d).

* * *

(4) Annual information return (i) In general. Except as described in paragraph (b)(4)(ii) of this section, the term annual information return includes an exact copy of any return filed by a tax-exempt organization pursuant to section 6033. It also includes any amended return the organization files with the Internal Revenue Service after the date the original return is filed. Returns filed pursuant to section 6033 include Form 990, Return of Organization Exempt From Income Tax, Form 990-PF, Return of Private Foundation, or any other version of Form 990 (such as Forms 990-EZ or 990-BL, except Form 990-T) and Form 1065. Each copy of a return must include all information furnished to the Internal Revenue Service on the return, as well as all schedules, attachments and supporting documents. . . .

Section 607(a) of the Tax Law provides:

General. Any term used in this article shall have the same meaning as when used in a comparable context in the laws of the United States relating to federal income taxes, unless a different meaning is clearly required but such meaning shall be subject to the

exceptions or modifications prescribed in this article or by statute. Any reference in this article to the laws of the United States shall mean the provisions of the internal revenue code of nineteen hundred eighty-six (unless a reference to the internal revenue code of nineteen hundred fifty-four is clearly intended), and amendments thereto, and other provisions of the laws of the United States relating to federal income taxes, as the same may be or become effective at any time or from time to time for the taxable year.

Opinion

A partnership is a conduit for New York State income tax purposes. Conduit treatment for partnerships means that any partnership items of income, gain, loss, deduction, and credit (e.g., investment tax credit) pass through to the partner and are claimed on the partner's tax return.

Pursuant to section 607(a) of the Tax Law, any term used for purposes of the New York personal income tax shall have the same meaning as used in the laws of the United States relating to federal income taxes unless a different meaning is clearly required.

A religious or apostolic organization described in section 501(d) of the IRC is exempt from federal income tax under section 501(a) of the IRC. Section 1.6033-1(a)(5)(i) of the Treasury Regulations provides that the organization must file federal Form 1065, *U.S. Return of Partnership Income*, to report its taxable income. The filing instructions for Form 1065 provide that an IRC section 501(d) organization must determine its taxable income in the same manner as a corporation. Section 501(d) of the IRC provides that each member of a section 501(d) organization must include his or her entire pro rata share of the organization's taxable income on his or her personal income tax return. The pro rata share included in the member's federal gross income is treated as a dividend. Accordingly, the character of the organization's items of income and deduction is not passed through to its members.

Petitioner is a corporation. The mere filing of a partnership return does not mean that Petitioner, as a 501(d) organization, is in fact a partnership for federal income tax purposes (see *Blume v Gardner*, 262 F Supp 405, affd, 397 F 2d 809 [6th Cir 1968]). The partnership tax return allows the Internal Revenue Service (IRS) to determine how much income must be reported by a section 501(d) organization's members. In *Kleinsasser v United States*, 707 F 2d 1024 (9th Cir 1983), the court held, in pertinent part, that members of a 501(d) organization were not entitled to the federal investment tax credit on farm equipment and machinery purchased by the organization because 501(d) organizations are not partnerships. Further, section 7701(a)(2) of the IRC defines a partnership as an unincorporated business. An incorporated organization cannot be a partnership for federal income tax purposes. (see *O'Neill v United States*, 410 F 2d 888, 893 [10th Cir 1969]). Lastly, a member's share of a 501(d) organization's income constitutes a dividend received and, as such, is not considered a distributive share of partnership

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gross income subject to the federal tax on net earnings from self-employment. (See IRS Revenue Ruling 58-328, 1958-1 C.B. 327.)

Accordingly, Petitioner is not a partnership for New York State income tax purposes, and the individual members of Petitioner are not allowed a pass-through of any tax credits or other tax incentives that may be accrued by Petitioner.

DATED: April 13, 2007

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