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

TSB-A-91 (4) I
Income Tax
January 29, 1991

STATE OF NEW YORK

COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. I901211B

On December 11, 1990 a Petition for Advisory Opinion was received from Buffalo Brass Company, Inc. c/o Richard F. Campbell, Esq., Hodgson, Russ, Andrews, Woods & Goodyear, 1800 One M&T Plaza, Buffalo, New York 14203.

The issue raised by Petitioner, Buffalo Brass Company, Inc., is whether shareholders of Petitioner may deduct their pro rata share of the business corporation franchise tax imposed by Chapter 190 of the Laws of 1990 on Petitioner, a subchapter "S" corporation for New York State tax purposes.

Petitioner is a foreign corporation doing business in New York State, as well as other states. Petitioner's shareholders have made an election to have Petitioner treated as a pass-through entity under subchapter S of the Internal Revenue Code. Petitioner's shareholders have also made an election to be treated as an "S" corporation for New York State tax purposes under Section 660 of the Tax Law. Petitioner recognized positive taxable income during its 1990 tax year. The amount of Petitioner's entire net income allocated to New York State for its 1990 tax year exceeds $300,000.

In 1990 New York State enacted provisions which impose a corporate-level tax on New York S corporations. The corporate-level tax is imposed under the Article 9-A Franchise Tax on Business Corporations. The tax imposed is the higher of a tax calculated on the basis of a fixed-dollar minimum pursuant to Section 210.1(d) of the Tax Law, or on the basis of entire net income allocated to New York pursuant to Section 210.1(a) of the Tax Law. See Tax Law §210.1(g), added by 1990 N.Y. Laws Ch. 190, §12. Petitioner's entire net income allocable to New York State for 1990 is at a level which guarantees that the corporate-level tax paid will be calculated on the basis of entire net income allocable to New York State.

Also enacted in 1990 was a temporary surtax which was imposed upon New York S corporations. The provisions relating to imposition of the surtax are also contained in the Article 9-A Franchise Tax on Business Corporations. The amount of surtax depends wholly upon the amount of tax calculated pursuant to the preceding paragraph. Thus, if the tax calculated pursuant to the preceding paragraph is based on entire net income allocated to New York the surtax will also be indirectly based on entire net income allocated to New York. Tax Law §209-A, added by 1990 N.Y. Laws Ch. 190, §31.

The corporate-level tax and the surtax will be deductible by Petitioner in calculating its income for federal tax purposes either as state taxes paid in the

pursuance of a trade or business activity pursuant to Section 164(a) of the Internal Revenue Code or as ordinary and necessary business expenses pursuant to Section 162 of said code. Since Petitioner is an S corporation for federal tax purposes, its income and deductions are taken into account and taxed at the shareholder level for federal tax purposes. The amount of Petitioner's income taken into account by Petitioner's shareholders for federal tax purposes will be reduced to reflect Petitioner's deductions for the New York State corporate-level tax and surtax.

> TSB-M-84-(8.5)-C issued December 29, 1988 provides in part as follows:
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> Section 607(a) of the Tax Law provides that any term used in Article 22 of the Tax Law shall have the same meaning as when used in a comparable context in the Internal Revenue Code, unless a different meaning is clearly required. Section 164(a)(3) of the Internal Revenue Code allows a deduction for: "State and local, and foreign, income. . . taxes." In determining what constitutes an "income tax" under section 164(a)(3) of the Code, the federal courts agree that such a tax must be a "net income tax"; that is, a direct tax on gain or profits, and that gain is a necessary ingredient of income. See Stratton's Independence, Ltd. v. Howbert, 231 US 399, 415; Eisner v. Macomber, 252 US 189, 207; and Bank of America National T. & S. Assoc. v. US, 459 F.2d 513, 517-8.
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> The New York State Corporate Franchise Tax and the New York City General Corporation Tax are not "income taxes" within the above definition. Northern Finance Corp. v. Tax Commission, 290 U.S. 601, 54 Sup. Ct. 230; and Matter of Bankers Trust New York Corporation v. Department of Finance, 120 AD 2d 992, 502 N.Y.S. 2d 567. Accordingly, shareholders of electing New York S corporations, in determining New York adjusted gross income, are not required to add to federal adjusted. . . gross income their pro rata share of the S corporation's deduction for these taxes, and may not subtract from federal adjusted gross income their pro rata share of the S corporation's refunds of these taxes.

The Taxes imposed on New York "S" corporations by Chapter 190 of the Laws of 1990 are "franchise" taxes and not "income" taxes. Therefore in accordance with the provisions of TSB-M-84(8.5)-C shareholders of Petitioner will not be required on their New York State personal income tax returns to add back to their federal adjusted gross income their pro rata share of any deductions taken by

Petitioner on its federal income tax return for corporation franchise taxes paid to New York State pursuant to Chapter 190 of the Laws of 1990.

DATED: January 29, 1991

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

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