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

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Corporation Tax
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Income Tax
June 3, 2002

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. Z010525B

On May 24, 2001, a Petition for Advisory Opinion was received from D'Amato & Lynch, Reserve Escrow Agent Under In re Bennett Funding litigation settlement, 70 Pine Street, New York, New York 10270.

The issues raised by Petitioner, D'Amato & Lynch, Reserve Escrow Agent Under In re Bennett Funding litigation settlement, are:

1. Whether the settlement fund described below is a corporation subject to taxation under Article 9-A of the Tax Law.

2. Whether the settlement fund described below is treated as a trust for purposes of Article 22 of the Tax Law.

3. Whether the settlement fund described below is subject to the New York City personal income tax authorized under Article 30 of the Tax Law.

4. Whether the settlement fund described below has any New York State franchise tax or New York State or City personal income tax filing or reporting obligations.

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

A settlement fund was created by an order dated July 25, 2000, of the United States District Court, Southern District of New York, in the In re Bennett Funding Group, Inc, securities litigation. That order, entitled Preliminary Order (Proposed) was, in effect, made final by the Final Order and Judgement (Number 1) Pursuant to Rule 54(b) Approving Settlement and Compromise of Class Claims Against Mahoney Cohen & Company, CPA, PC.

The Preliminary Order (Proposed) provides that on April 29, 1997, the Court certified the action (MDL No. 1153 (JES), Civil Action No. 96-CIV-2583) (the "Consolidated Action") to proceed as a class action under Rules 23(a) and (b)(3) of the Federal Rules of Civil Procedure ("Fed R Civ P") on behalf of all persons and entities who purchased or invested in BFG[1] Securities

[1] "BFG" is the Bennett Funding Group, Inc., Bennett Management and Development Corporation, Bennett Receivables Corp., Bennett Receivables Corp. II, Aloha Capital Corporation, The Processing Center, Inc., American Marine International, Ltd., and Resort

that were offered by or on behalf of BFG or any of its related entities, or who "rolled over" investments into BFG Securities. The class and/or subclasses include persons and entities who purchased or invested in BFG Securities or rolled over investments during the period March 29, 1992 through March 29,1996 (the "Plaintiff Class"). In June 2000 the Plaintiff Class, and Richard C. Breeden, the BFG Trustee as plaintiff on behalf of BFG and the Estate in two proceedings (an adversary proceeding in the United States Bankruptcy Court for the Northern District of New York, entitled *Breeden v Bennett*, Adv Pro No. 96-70154 (the "First Adversary Proceeding") and another adversary proceeding in the same court entitled *Breeden v Mahoney Cohen & Co., P.C.*, Adv Pro No. 98-70617A ("Second Adversary Proceeding"), and Mahoney Cohen & Company, CPA, PC ("Mahoney") entered into a Stipulation and Agreement of Settlement ("Stipulation"), which is subject to review under Fed R Civ P Rule 23 as it relates to the Consolidated Action.

The Stipulation and the settlement comprised therein (the "Settlement") were expressly conditioned upon a final and non-appealable order of the Court approving the Settlement, a judgment of dismissal with prejudice and a release of all claims against Mahoney pertaining in any manner to BFG, the Estate, or the BFG Securities, and a determination that the Settlement is binding upon all persons and entities who purchased or invested in BFG Securities from March 29, 1992 through March 29, 1996 (including heirs, transferees and assigns of such persons) and who did not request complete exclusion from the Plaintiff Class in the manner and within the time provided by the Class Certification Order. Pursuant to the Stipulation, an Escrow Agreement has been filed which provides that a specific portion of the amount to be paid on behalf of Mahoney by its Insurer pursuant to the Settlement is to be put in escrow for use by Mahoney in connection with other claims and potential claims against Mahoney affecting the same policy year (the "Claims Reserve Amount").

The Escrow Agreement was made and entered into in June 2000 by and among the plaintiffs and the certified class in the Consolidated Action, the BFG Trustee, Mahoney, The Garden City Group, Inc. (the "Proceeds Escrow Agent") and Petitioner (the "Reserve Escrow Agent"). Pursuant to the terms of the Stipulation, Mahoney shall cause to be placed in escrow the remaining balance of Mahoney's insurance policy with its insurer. Of this balance, the Claims Reserve Amount will be paid over to the Reserve Escrow Agent. The remaining amount (the "Proceeds Amount") will be paid over to the Proceeds Escrow Agent. These payments collectively constitute a settlement fund to be deposited and held in separate escrow accounts (the "Escrow Accounts") with interest earned thereon and other authorized additions or reductions (the "Escrow Amounts").

Paragraphs one and two of the Escrow Agreement provide that the Proceeds Escrow Agent shall establish a separate Escrow Account for the Proceeds Amount and the Reserve Escrow Agent shall establish a separate Escrow Account for the Claims Reserve Amount. All Escrow Amounts

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Service Company, Inc. Bankruptcy proceedings involving these entities were substantively consolidated and their consolidated estate is referred to below as the "Estate."

held in the Escrow Accounts shall be invested or reinvested by the Escrow Agents in instruments, or in money market mutual funds investing solely in instruments, secured by the full faith and credit of the United States, including Treasury Bills, Treasury Notes, and Treasury Bonds, or in instruments constituting obligations issued or guaranteed by agencies or instrumentalities of the United States. The Escrow Agents may sell such investments from time to time, as required, to disburse funds in accordance with the Escrow Agreement. All such investments (including principal, interest, and sale proceeds) shall at all times constitute a part of the Escrow Amounts, and all income and profits on such investments shall be credited to, and losses thereon shall be charged against, the Escrow Amounts.

Paragraph four of the Escrow Agreement provides that the Reserve Escrow Agent may make payments out of the Claims Reserve Amount on account of Reserve Claims and may make other payments authorized herein or in the Stipulation, upon presentation of bills, requisitions or other requests for payment. However, prior to such payments being made, the Reserve Escrow Agent shall provide written notice to Co-Lead Counsel and counsel for the Trustee. If there is no objection within seven days, the Reserve Escrow Agent shall make such payments. Such payments shall be chargeable against the Claims Reserve Amount starting on the date as of which the Stipulation has been submitted to both the District Court and the Bankruptcy Court. It is expressly understood and consented to that Petitioner, as the Reserve Escrow Agent, may be making payments to itself for services and disbursements in that capacity, and in its capacity as counsel for Mahoney in all BFG-related matters. Payments from the Claims Reserve Amount for settlement or judgments on Reserve Claims shall be made at the rate of $.90 per dollar of settlement or judgment amount. Payments for the reasonable expenses authorized by paragraphs VIII. A. and C. of the Stipulation shall be made at the rate of 100 cents per dollar. Nothing in the Escrow Agreement shall be deemed to be a limitation on Mahoney's complete discretion to make payments from the Claims Reserve Amount authorized by the Stipulation and the Escrow Agreement.

The settlement fund in this case is a "qualified settlement fund" as defined in section 1.468B-1 of the federal Treasury Regulations. The settlement fund has filed a federal Form1120-SF, United States Income Tax Return for Settlement Funds (Under Section 468B), for the taxable year ended December 31, 2000, but has not filed any New York State or City returns.

Discussion

Issue 1

Under section 468B of the Internal Revenue Code, a qualified settlement fund is treated as a corporation for federal tax administrative and procedural purposes.

Pursuant to section 1.468B-1(a) and (c) of the Treasury Regulations, a qualified settlement fund, for federal income tax purposes, is a fund, account or trust that satisfies the following requirements:

(1) It is established pursuant to an order of, or is approved, by the United States or another governmental authority, and is subject to the continuing jurisdiction of that governmental authority.

(2) It is established to resolve or satisfy one or more contested or uncontested claims that have resulted or may result from an event that has occurred and that has given rise to at least one claim asserting liability (i) under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, (ii) arising out of a tort, breach of contract, or violation of law, or (iii) designated by the Commissioner of Internal Revenue in a revenue ruling or revenue procedure.

(3) The fund, account or trust is a trust under applicable state law, or its assets are otherwise segregated from other assets of the transferor (and related persons).

Section 209.1 of the Tax Law imposes, annually, a franchise tax on every corporation for the privilege of exercising its corporate franchise, or of doing business, or of employing capital, or of owning or leasing property in New York State in a corporate or organized capacity, or of maintaining an office in New York State for all or any part of each of its fiscal or calendar years.

Section 208.1 of the Tax Law provides, in part, that:

> The term "corporation" includes (a) an association within the meaning of paragraph three of subsection (a) of section seventy-seven hundred one of the internal revenue code ... (b) a joint-stock company or association, (c) a publicly traded partnership treated as a corporation for purposes of the internal revenue code pursuant to section seventy-seven hundred four thereof and (d) any business conducted by a trustee or trustees wherein interest or ownership is evidenced by certificate or other written instrument ....

The term "corporation" is defined in section 1-2.5 of the Business Corporation Franchise Tax Regulations, which provides, in part, that:

> (a) The term 'corporation' means an entity created as such under the laws of the United States, any state, territory or possession thereof, the District of Columbia, or any foreign country, or any political subdivision of any of the foregoing, which provides a medium for the conducting of business and the sharing of its gains.

* * *

(b) ... An entity conducted as a corporation is deemed to be a corporation.

* * *

(2) A business conducted by a trustee or trustees in which interest or ownership is evidenced by certificate or other written instrument includes, but is not limited to, an association commonly referred to as a business trust or Massachusetts trust. In determining whether a trustee or trustees are conducting a business, the form of the agreement is of significance but is not controlling. The actual activities of the trustee or trustees, not their purposes and powers, will be regarded as decisive factors in determining whether a trust is subject to tax under article 9-A of the Tax Law. The mere investment of funds and the collection of income therefrom, with incidental replacement of securities and reinvestment of funds, does not constitute the conduct of a business in the case of a business conducted by a trustee or trustees.

For New York State franchise tax purposes, an unincorporated entity is not taxed as a corporation unless its activities are conducted in a manner whereby the entity presents itself as a corporation, in which case it is deemed to be a corporation. See Fibreboard Asbestos Compensation Trust, Adv Op Comm T&F, January 21, 1997, TSB-A-97(3)C and (1)I; The Steinhardt-Caxton Consolidated Settlement Fund, Adv Op Comm T & F, August 3, 1995, TSB-A-95-(14)C and (5)I.

The conduct of business is more than the ownership of property and the collection and distribution of income derived from that property. (Smadbeck v St Tax Comm, 33 NY2d 930 (1973); People ex rel Nauss v Graves, 283 NY 383, 386 (1940)). It is "more than the mere investment of funds and the collection of income therefrom, with the incidental replacement of securities and the reinvestment of funds that constitute the corpus, as in the case of an ordinary trust". (Burrell v Lynch, 274 AD 347, 352 (1948); see also, City Bank Farmers Trust Co. v Graves, 272 NY 1, 6 (1936)).

Herein, the activities of the settlement fund do not constitute the conduct of a business as contemplated by section 208.1 of the Tax Law and section 1-2.5 of the Business Corporation Franchise Tax Regulations. See Fibreboard Asbestos Compensation Trust, supra; The Steinhardt-Caxton Consolidated Settlement Fund, supra; and Samuel R. Buxbaum, Administrator Buxbaum-Banco Popular Settlement Fund, Adv Op Comm T & F, April 30, 1993, TSB-A-93(10)C and (5)I.) Accordingly, the settlement fund is not deemed to be a corporation for purposes of Article 9-A of the Tax Law, and is not subject to the tax imposed by such Article.

Issue 2

The New York State personal income tax under Article 22 of the Tax Law is imposed on resident and nonresident trusts.

Section 607(a) of the Tax Law provides, in pertinent part, that:

> [a]ny 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 ....

For federal income tax purposes, the settlement fund in this case is a qualified settlement fund. Pursuant to section 1.468B-1(b) of the Treasury Regulations, a fund, account, or trust that is a qualified settlement fund that could be classified as a trust within the meaning of section 301.7701-4 of the Treasury Regulations, is classified as a qualified settlement fund for all purposes of the Internal Revenue Code ("IRC"). Accordingly, since the settlement fund is not treated as a trust for federal income tax purposes, the settlement fund pursuant to section 607(a) of the Tax Law, is not treated as a trust for purposes of Article 22 of the Tax Law. (See, Steinhardt-Caxton, supra, and Samuel R. Buxbaum, supra.) Therefore, the settlement fund is not subject to the tax imposed under Article 22 of the Tax Law.

Issue 3

The New York City personal income tax is similar to the New York State personal income tax and is administered by New York State the same as Article 22 of the Tax Law. Accordingly, the settlement fund in this issue is not treated as a trust for New York City personal income tax purposes and the settlement fund is not subject to the New York City personal income tax authorized under Article 30 of the Tax Law.

Issue 4

After determining that the settlement fund in this issue is not a taxable entity for New York State and New York City tax purposes, the settlement fund has no New York State franchise tax or New York State or New York City personal income tax filing or reporting obligations.

DATED: June 3, 2002

/s/
Jonathan Pessen
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Technical Services Division

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