

May 16, 2001

**Re:** Request for Ruling  
Commercial Rent Tax

FLR-014774-007

Dear Mr. \_\_\_\_\_ :

This is in response to your request for a ruling dated March 14, 2001 regarding the application of the New York City Commercial Rent Tax ("CRT") to the office space that the \_\_\_\_\_ ("Taxpayer") has leased at \_\_\_\_\_, New York, New York (the "Taxpayer's premises" or the "premises"). Additional information was received on or about April 10, 2001.

#### FACTS

The facts presented are as follows:

The Taxpayer is a non-profit membership organization exempt from federal income taxes under section 501(c)(4) of the Internal Revenue Code ("IRC"). You have represented that the Taxpayer exists to serve the needs and interests, and enhance the quality of life, of persons 50 years of age and older. In furtherance of these objectives, the Taxpayer engages in education and advocacy activities and provides services and programs for persons in the above age category.

The Taxpayer's members receive a copy of a bimonthly magazine as a part of their membership. Prior to 2001, all members received the publication \_\_\_\_\_ (the "original publication"). In February, 2001, the Taxpayer launched a new publication known as \_\_\_\_\_ (the "new publication") directed at members between the ages of 50 and 55 who are all part of the post war "baby boom" generation. These baby boom members of the Taxpayer now receive the new publication instead of the original publication. In the years following 2001, the top end of the age group receiving the new publication will increase by one year so that the members that receive the new publication will continue to receive the new publication after reaching age 55. Hence, in 2002, members of the Taxpayer between the ages of 50 and 56 will receive the new publication, and, in 2003,

members between the ages of 50 and 57 will receive the new publication. Members of the Taxpayer who do not receive the new publication as part of their membership will continue to receive the original publication which will now be directed at older members. However, these members who wish to receive the new publication may purchase an annual subscription to it for ten dollars. This subscription fee is in addition to the regular membership dues for these members. Also, the new publication will be available on newsstands in a limited number of cities across the country.

You have represented that all editorial staff and activities for the new publication are located at the premises and that the editorial staff and activities for the original publication, and the advertising solicitations and marketing activities for both the new and original publications are conducted at a second location in New York City. Further, you have represented that, for federal income tax purposes, the Taxpayer will treat the income generated from the sale of advertisements in the new publication as unrelated business income. However, the Taxpayer will treat the circulation income from the new publication, including any revenue from subscription and newsstand sales of this publication, as tax-exempt income, rather than unrelated business income. You have also represented that the circulation income from the new publication is tax exempt because the publication “contributes importantly to the accomplishment of the [Taxpayer’s] exempt purpose” because it provides “informational content that is relevant to addressing the needs and interests of persons over 50 and thereby [enhances] the quality of life for all by promoting independence, dignity and purpose for such persons.”

## ISSUE

You have requested a ruling as to whether the Taxpayer’s use and occupancy of the premises are subject to the CRT.

## CONCLUSION

We have concluded that the Taxpayer’s use and occupancy of the premises are not subject to the CRT because the premises are not taxable premises.

## DISCUSSION

The CRT is imposed on a tenant who occupies, uses, or intends to occupy or use premises in New York City for “carrying on or exercising any trade, business, profession, vocation or commercial activity....” Administrative Code of the City of New York (“Code”) §§11-701(5), 11-701(7) and 11-702(a)<sup>1</sup>. A “tenant” is defined as a “person paying or required to pay rent for premises as a lessee, sublessee, licensee, or concessionaire.” Code § 11-701(3). The Taxpayer is clearly a “tenant” of the premises under section 11-701(3). Hence, the Taxpayer’s use and occupancy of the premises will be subject to the

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<sup>1</sup> For periods beginning on or after September 1, 1995, the rent on any premises located in boroughs other than the Borough of Manhattan or located north of the center line of Ninety-Sixth Street in the Borough of Manhattan is exempt from the CRT. Code § 11-704(h)(1).

CRT if the Taxpayer occupies or uses the premises in connection with a “trade, business, profession, vocation, or commercial activity...” and the Taxpayer is not otherwise exempt from the CRT. Code § 11-701(5).

Code section 11-704(a)(4) exempts from the CRT any organization “organized and operated exclusively for religious, charitable, or educational purposes, or for the prevention of cruelty to children or animals, and no part of the net earnings of which inures to the benefit of any private shareholder or individual and no substantial part of the activities of which is carrying on propaganda or otherwise attempting to influence legislation...” However, the Taxpayer does not qualify for the exemption under section 11-704(a)(4), because the Taxpayer is exempt from federal income taxation under IRC section 501(c)(4), as a not for profit organization operated exclusively for the promotion of social welfare, and not as an educational, charitable or religious organization under IRC section 501(c)(3). None of the other exemptions to the CRT are applicable to the Taxpayer. See Code § 11-704.

The Taxpayer has represented that the premises will be used for the editorial staff and activities of the new publication, and that advertising activities for the new publication will be conducted at a second location and not at the premises. Accordingly, whether the Taxpayer’s use and occupancy of the premises are exempt from the CRT turns on whether the Taxpayer’s editorial activities constitute a business, trade, profession or commercial activity.

Under section 7-06 of Title 19 of the Rules of the City of New York (“RCNY”), all premises are presumed to be taxable. The tenant bears the burden of proof in showing that the tenant does not use its premises in connection with the conduct of a business, trade, profession or commercial activity. See 19 RCNY § 7-06. However, with certain exceptions not relevant here, premises used or occupied by an organization exempt under IRC section 501 are presumed not to be taxable premises unless the premises are used “substantially in connection with an unrelated trade or business.” 19 RCNY § 7-06. Hence, if the premises are not used “substantially in connection with an unrelated trade or business,” the Taxpayer’s use of the premises is presumed not to be in connection with a business, trade, profession or occupation that would subject the Taxpayer to the CRT. Inasmuch as 19 RCNY section 7-06 adopts the federal income tax concept of unrelated trade or business, it is appropriate to use federal income tax law analysis to determine whether the Taxpayer’s activities on the premises constitute an unrelated trade or business.

Tax-exempt organizations are subject to federal income tax on unrelated business income. IRC §§ 511, 512, 513. To determine unrelated business income under the IRC, the Treasury Regulations follow the “fragmentation principle”. Under that principle, the “circulation income” generated by the distribution of the editorial or readership content of a tax exempt organization’s publication must be separated from the “advertising income” generated by the sale of advertising space in that publication. See Treas. Reg. §§1.512(a)-1(f), 1.513-1(d); United States v. American College of Physicians, 475 U.S. 834, 839-840 (1986); American Medical Ass’n v. United States, 887 F.2d 760, 763 (7<sup>th</sup> Cir. 1989).

Circulation income includes income from the sale or distribution of the publication as well as an allocated portion of the membership dues of the tax-exempt organization, if the right to receive the publication is included with membership in the organization. See Treas. Reg. §§1.512(a)-1(f)(3), 1.512(a)-(1)(f)(4).

Where the publication's editorial content contributes importantly to the tax-exempt organization's exempt purpose, the publication's circulation income is tax-exempt income, and is not taxable unrelated business income. See Treas. Reg. §§ 1.513-1(d)(2), 1.513-1(d)(4); American Medical Ass'n, at 763. By contrast, the tax-exempt organization's income from advertising activities is considered unrelated business income, unless the Taxpayer's conducting of an advertising business contributes importantly to the organization's exempt purpose. See Treas. Reg. § 1.513-1(d)(4)(iv) Examples 5 & 7. The content of the advertisements is not determinative.

Here, the Taxpayer has represented that the editorial content of the new publication "contributes importantly to the accomplishment of the taxpayer's exempt purpose" because it provides "informational content that is relevant to addressing the needs and interests of persons over 50 and thereby [enhances] the quality of life for all by promoting independence, dignity and purpose for such persons." The Taxpayer has also represented that it will treat the new publication's circulation income as tax-exempt income, rather than unrelated business income, for federal income tax purposes. In addition, the Taxpayer's tax-exempt treatment of the circulation income from the new publication is fully consistent with its treatment of the circulation income from its other publications on its recent federal income tax returns.<sup>2</sup>

Based on the Taxpayer's representations and its consistent federal income tax reporting practices, we conclude that the circulation income from the new publication is not unrelated business income, and that the taxpayer's editorial activities do not constitute an unrelated trade or business. Accordingly, under 19 RCNY section 7-06, the Taxpayer's use of the premises for its editorial activities is presumed not to be in connection with a trade or business. Given the Taxpayer's representations and the above presumption, we conclude that the Taxpayer's use and occupancy of the premises are not subject to the CRT.

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<sup>2</sup> The Taxpayer will report its advertising income from the new publication as unrelated business income, and it has consistently done the same with respect to its other publications.

The Department reserves the right to verify the information submitted. In addition, you must notify the Department immediately if the circulation income from the new publication is ever treated as unrelated business taxable income for federal income tax purposes. You must also notify the Department immediately if there is any change in the nature of the activities conducted at the Taxpayer's premises.

Sincerely,

Devora B. Cohn  
Associate Commissioner  
For Legal Affairs