



FINANCE
NEW • YORK
THE CITY OF NEW YORK
DEPARTMENT OF FINANCE

October 15, 2003

Re: Request for Ruling
Banking Corporation Tax

FLR# 034810-006

Dear _____ :

This is in response to your request dated August 26, 2003 for a ruling regarding the application of the issued capital stock tax base (described below) under the New York City Banking Corporation Tax ("Bank Tax") to _____ . (the "Taxpayer"), a bank, in the circumstances described below. Additional information was received on September 24, 2003.

FACTS

Taxpayer is a banking corporation organized under the laws of _____ that conducts business through a branch in New York City (the "City"), and is subject to the Bank Tax. Prior to the fiscal year ended _____, Taxpayer had outstanding par value stock. During the fiscal year ended _____, _____ changed its laws to eliminate par value stock, and Taxpayer's par stock became no par stock. Consequently, Taxpayer believes that its Bank Tax liability for the fiscal year ended _____, based on its issued capital stock may exceed the Bank Tax liability Taxpayer would owe under the highest applicable tax base determined as if had Taxpayer been organized in the United States (a "domestic bank").

ISSUE

You have requested a ruling as to whether the Bank Tax based on issued capital stock as applied to Taxpayer violates the U.S.- _____ Tax Treaty when the tax computed on the issued capital stock base is greater than the tax calculated under the highest base that would be applicable if Taxpayer were a domestic bank.

CONCLUSION

Based on the facts presented, the Bank Tax computed on issued capital stock, as applied to Taxpayer, violates the U.S.- Tax Treaty, only if Taxpayer's Bank Tax liability is greater than the tax calculated on whichever tax base would result in the highest tax if Taxpayer were a domestic bank.

DISCUSSION

The Administrative Code of the City of New York (the "Code") imposes the Bank Tax at the highest of nine percent of a taxpayer's entire net income allocated to the City ("allocated entire net income") or one of several alternative taxes (collectively with the tax on entire net income, the "applicable taxes"). *See* Code § 11-643.5. For domestic banks, the starting point for determining allocated entire net income is worldwide income. *See* Code § 11-641(a)(1); Internal Revenue Code ("IRC") §§ 61, 63. One of the alternative applicable taxes for domestic banks is computed on the domestic bank's allocated asset base. This tax is imposed at a rate of one-tenth of a mill for every dollar of allocated assets. Code § 11-643.5(b)(1). Under the applicable provisions of the Rules of the City of New York ("RCNY"), real and tangible personal property are to be valued at cost while loans, investments and other intangible property assets must be valued at book value for purposes of calculating the tax due. *See* Title 19 RCNY § 3-03(e)(2)(iii). The other applicable taxes for domestic banks are a tax of three percent of taxpayer's alternative entire net income allocated to the City ("allocated alternative entire net income")¹ and a minimum tax of \$125. Code §§ 11-643.5(b)(3), 11-643.5(b)(4).

For alien banks, *i.e.* banks organized under the laws of a country other than the United States, the starting point for determining both allocated entire net income and allocated alternative entire net income is effectively connected income and not worldwide income. *See* Code § 11-641(a)(3); IRC § 882. In addition, alien banks are not subject to the tax on the allocated asset base. Rather, alien banks are subject to an alternative tax based on the value of the alien bank's issued capital stock. The capital stock-based tax is imposed at a rate of 2.6 mills for each dollar of value of the alien bank's issued capital stock. Code § 11-643.5(b)(2)(i). If the stock has a par value, the tax is calculated using the par value, but, if the stock does not have par value, the tax is calculated using the actual or market value of the stock, but the market value cannot be less than \$5 per share.² *Id.*

Taxpayer asserts that its liability under the capital stock-based tax is higher than what its liability would have been had its bank tax been calculated under the highest base applicable to a domestic bank.

The United States and are parties to the Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, U.S.- , art. , U.S.T. (hereinafter the "Treaty"). Article of the Treaty provides in part: "A permanent establishment which a resident of a Contracting State has in the other

¹ Alternative entire net income allocated to the City is determined in the same way as entire net income except that certain interest and dividend income that is deducted in determining entire net income is not deducted for purposes of alternative entire net income. *See* Code §§ 11-641.1, 11-641(e)(11) & (12).

² The \$ 125 minimum tax is the same for alien banks as it is for domestic banks. *See* Code § 11-643.5(b)(4).

Contracting State shall not be subjected in that other Contracting State to *more burdensome taxes than a resident of that other Contracting State carrying on the same activities.*” Treaty, art., ¶ (2) (emphasis added) (hereinafter the “non-discrimination provision”). Under article of the Treaty, a corporation is a resident of . Treaty, art. 3, ¶ (1)(a). Article of the Treaty, which defines the term “permanent establishment” includes a branch within the meaning of that term. *Id.*, art. , ¶¶ 1, 2(c). Accordingly, Taxpayer is entitled to the protection afforded by the Treaty’s nondiscrimination provision.

Under article of the Treaty, article , the non-discrimination provision, applies to “taxes of every kind imposed by a Contracting State *or a political subdivision or local authority thereof.*” Treaty, art. , ¶(3) (emphasis added). The Treaty defines terms “Contracting State and the “other Contracting State” to mean the United States or , as the context requires. *Id.*, art. 2, ¶(1)(c). Accordingly, the Bank Tax is subject to article of the Treaty.

The quoted language from article does not specify whether the relevant comparison for purposes of the Treaty is between a Japanese corporation and a corporation incorporated in the United States (a “U.S. corporation”) carrying on the same activities, or between the U.S. branch of the corporation and a U.S. corporation that is carrying on the same activities. However, case law and other authority suggest that, for purposes of the Bank Tax, the relevant comparison is between the tax imposed on a corporation with a branch in the City and the tax imposed on a U.S. corporation with a branch in the City that is carrying on the same activities. *See Matter of Reuters Ltd. v. Tax Appeals Tribunal*, 82 N.Y.2d 112, 116 (1993) (“[T]he purpose of the nondiscrimination clause is to protect foreign taxpayers against local economic discrimination derived from disparate tax treatment. The ultimate taxpayer ... is the corporate entity ... not its branch affiliate. Thus, ... the potential discriminatory effect of New York’s franchise tax [cannot be measured] by reference to ... [a] New York branch as an enterprise discrete from its ... parent....”) The nondiscrimination language in the U.S.-U.K. tax treaty at issue in *Reuters* is very similar to the nondiscrimination provision. *See also* Commentary on Organization for Economic Cooperation and Development Model Tax Treaty (“OECD Commentary”), Article 24, ¶¶ 36, 37, 38 (2001) (taking into account the income of the entire alien entity does not offend a non-discrimination clause if a domestic entity is taxed in the same way); OECD Commentary, Article 24, ¶¶ 38, 39, 40 (1977) (same).³

In our opinion, Article of the Treaty precludes the City from imposing a greater Bank Tax liability on a bank with a branch in the City than would apply to the same bank if it were a domestic bank. *See Reuters*, at 116; *Lufthansa v. City of New York*, 57 A.D.2d 533 (1st Dept. 1977) *affg. for the reasons stated at* 85 Misc.2d 719 (Supreme Court, New York County 1976). A domestic bank is subject to the highest of the four applicable taxes under section 11-643.5. Accordingly, the non-discrimination provision will apply if the Taxpayer can establish that its highest applicable tax liability as an alien bank is greater than its highest applicable tax liability calculated under all of the applicable taxes as if Taxpayer, and not just the City branch, were a domestic bank. *See*

³ The OECD Commentaries are for a model treaty that contains a non-discrimination provision very similar to the one in the Treaty.

Reuters, 82 N.Y.2d at 116; OECD Commentary, article 24, ¶¶ 37, 38 (2001); OECD Commentary, article 24, ¶¶ 39, 40 (1977). Any such factual assertion by Taxpayer is subject to audit and is not within the scope of the Letter Ruling function. *See* 19 RCNY §16-01(c)(5).

Sincerely,

Ellen E. Hoffman
Assistant Commissioner for Tax Law & Conciliations

JJM:jm