New York City Tax Appeals Tribunal

In the Matter of	:	
	:	DECISION
NATIONAL BULK CARRIERS, INC. AND AFFILIATES	:	TAT (E) 04-33 (GC)
Petitioner.	:	

National Bulk Carriers, Inc. and Affiliates ("Petitioner") filed an exception (the "Exception") to a Determination of the Chief Administrative Law Judge ("CALJ") dated May 3, 2006 (the "CALJ Determination"). The CALJ Determination sustained a Notice of Determination, dated June 25, 2004, issued by the New York City Department of Finance (the "Department") to Petitioner (the "Notice"). The Notice asserted a New York City General Corporation Tax ("GCT") deficiency in the principal amount of $343,832.46 plus interest and penalties for the calendar years 1997, 1998 and 1999 (the "Tax Years").

Petitioner appeared by John W. Weber, Esq., Lori D. Guttentag, Esq., and John M. Aerni, Esq., of LeBoeuf, Lamb, Greene & MacRae LLP and the Commissioner of Finance of the City of New York (the "Commissioner" or "Respondent") appeared by George P. Lynch, Esq., Assistant Corporation Counsel, New York City Law Department. The Parties filed briefs and oral argument was held before this Tribunal. Commissioner Robert J. Firestone, Esq., did not participate in this Decision.

During the Tax Years, National Bulk Carriers, Inc., a New Jersey corporation, filed GCT combined reports with the following subsidiaries: (a) Hawaiian Realty, Inc.; (b) 605

Third Avenue Realty, Inc. (1997 only); (c) Hawaiian 605 Special Corp.; (d) HRI 605 Mezzanine Special Corp.; (e) 1345 Sixth Avenue Company, Inc.; (f) Hawaiian 1345 Special Leasehold Corp.; (g) Hawaiian 1345 Special Fee Corp.; and (h) Hawaiian 1345 Funding Corp. (collectively, the "Subsidiaries").[1] Each of the Subsidiaries was incorporated in New York State (the "State").

Certain Subsidiaries owned interests in several partnerships.[2] The assets held by the partnerships consisted of ownership of and leasehold interests in the land and buildings located at 605 Third Avenue and 1345 Sixth Avenue in New York City (the "City").

Some Subsidiaries owned, in the aggregate, a 50% membership interest in 605 Third Avenue LLC, a limited liability company that owned the land and building located at 605 Third Avenue.

Certain Subsidiaries owned, in the aggregate, a 0.5% general partnership interest and a 49% limited partnership interest in 1345 Fee Limited Partnership, a partnership that owned the land at 1345 Sixth Avenue.

Some Subsidiaries owned, in the aggregate, a 0.5% general partnership interest and a 49.5% limited partnership interest in 1345 Leasehold Limited Partnership, a partnership that owned a leasehold interest in the building at 1345 Sixth Avenue.

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[1] Except as noted below, the CALJ's Findings of Fact, although paraphrased and amplified herein, generally are adopted for purposes of this Decision.

[2] Although the partnerships include a limited liability company, the Parties agreed that ownership interests in partnerships and limited liability companies should be treated identically under the GCT.

The remaining interests in 605 Third Avenue LLC, 1345 Fee Limited Partnership and 1345 Leasehold Limited Partnership (collectively, the “Partnerships”) were owned by the Fisher Group, a group of commonly controlled entities. The Fisher Group and Petitioner are not related and are not owned directly or indirectly by the same persons. The 0.5% interests in the Partnerships owned by the relevant Subsidiaries were managing partnership interests that provided certain management rights. The Fisher Group was the other managing partner in the Partnerships.

Petitioner filed combined GCT returns (Form NYC-3A) for the Tax Years (the “Returns”). Petitioner included its distributive shares of the Partnerships’ income as shown on the federal Schedules K-1 in its entire net income (“ENI”) pursuant to § 11-602.8 of the New York City Administrative Code (the “Code”) for the Tax Years.

For the 1997 Tax Year, pursuant to Code § 11-604.1.E(a)(4), Petitioner reported its GCT liability as the minimum tax of $300 (the “Minimum Tax”) for the reporting corporation and each of the taxable corporations because it represented the greatest amount of tax. For the 1998 Tax Year and the 1999 Tax Year, Petitioner computed its GCT liability on its ENI pursuant to Code § 11-604.1.E(a)(1) (the “ENI Method”) because it yielded the greatest amount of tax. Although the Parties stipulated that “Petitioner computed the GCT owed on its combined reports using the capital base method . . .” (Stipulation para. 11) the audit workpapers prepared by the Department (Stipulation, Exhibit C) indicate that Petitioner reported its GCT liability for the 1997 Tax Year as the Minimum Tax and reported its GCT liability for the 1998 Tax Year and the 1999 Tax Year using the ENI Method. By a letter dated May 16, 2007, to the Tribunal Commissioners, Petitioner confirmed that its GCT liability for the 1997 Tax Year was reported as the Minimum Tax and that its GCT liability for the 1998 Tax Year was computed using the ENI Method. In that letter, Petitioner stated that its GCT liability for the 1999 Tax Year originally was computed under Code § 11-

604.1.E(a)(2) on the capital base (the "Capital Method") valuing its business capital using the fair market value of Petitioner's ratable share of the Partnerships' assets (the "aggregate approach"). However, Petitioner amended its 1999 Return to value its business capital using the value for the Partnership interests shown on Petitioner's books and records in accordance with generally accepted accounting principles ("GAAP") (the "entity approach") with the consequence that the GCT liability for that Tax Year was computed using the ENI Method.[3]

In calculating the property factor of its business allocation percentage ("BAP") pursuant to Code § 11-604.3(a)(1), Petitioner included its ratable share of the Partnerships' property valued at the Partnerships' adjusted basis for federal income tax purposes.[4]

The Notice issued by the Department to Petitioner asserted a total GCT deficiency for the Tax Years of $536,907.49 including principal of $343,832.46, interest of $158,691.79 computed through July 15, 2004, and a 10% substantial understatement of tax penalty of $34,383.24.

The Parties stipulated that "the [Notice] should be sustained" if Petitioner is required to include its ratable share of the Partnerships' property in its business capital valued at fair market value, but that "the [Notice should] be cancelled" if Petitioner is required to include

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[3] Notwithstanding the Parties' Stipulation (Stipulation para. 11), Petitioner did not calculate its GCT liability under the Capital Method for any of the Tax Years (other than on the original 1999 Return). Accordingly, because there is insufficient information in the Record to permit us to determine how Petitioner valued its business capital for its 1997 and 1998 Tax Years, the CALJ's Findings of Fact 7 and 9 are modified to more accurately reflect the Record.

[4] Petitioner did not elect to use fair market value in computing the property factor of its BAP as permitted by Code § 11-604.3(a)(1).

its interests in the Partnerships in its business capital valued under GAAP. Stipulation para. 14.[5]

The CALJ concluded that for purposes of computing Petitioner's business capital under the Capital Method, the aggregate approach should be applied to treat Petitioner as owning a ratable share of the Partnerships' real property. Thus, the CALJ sustained the Notice in full.

Petitioner contends that the assets to be valued in computing its GCT liability under the Capital Method pursuant to Code § 11-604.1.E(a)(2) are Petitioner's interests in the Partnerships and that because those interests are intangible personal property, Code § 11-604.2 requires its interests in the Partnerships to be valued at "the value thereof shown on [Petitioner's] books and records . . . in accordance with [GAAP]." Respondent counters that the assets to be valued in computing Petitioner's GCT liability under the Capital Method are Petitioner's ratable share of the assets of the Partnerships valued at fair market value pursuant to Code § 11-604.2.

Petitioner concedes that the aggregate approach applies to the ENI Method of computing GCT and the computation of the BAP because the Code specifically requires the use of that approach in those instances, but Petitioner contends that the Capital Method is "fundamentally different" from the ENI Method.[6] Respondent counters that the ENI Method and the Capital Method are not separate taxes but are two of the four alternative means of computing GCT liability. Petitioner also argues that the substantive distinction between a

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[5] The Notice includes a substantial understatement of tax penalty for each of the Tax Years. However, Petitioner did not contest the penalties. Based on the Stipulation (Stipulation para. 14) we have not addressed the penalties in this Decision.

[6] Exception at unnumbered page 5.

partnership interest and an interest in the partnership's underlying assets should be reflected in the calculation of GCT under the ENI Method and the Capital Method. Lastly, Petitioner asserts that its position is consistent with a non-precedential determination issued by an administrative law judge of the State Division of Tax Appeals (the "State Tribunal") under comparable statutory language in the State Tax Law and that, in the absence of a contrary ruling or pronouncement by the City, Petitioner correctly relied on that determination in preparing the Returns.

For the reasons set forth below, we affirm the CALJ Determination.

The GCT imposes a tax on every corporation doing business, owning or leasing property or engaging in various other activities in the City. Code § 11-603.1. The GCT is the sum of: (1) the greatest amount of tax calculated under four alternative methods; plus (2) an amount of tax calculated on subsidiary capital.[7] Code § 11-604.1.E. The three alternative methods relevant to the matter at bar are the Minimum Tax, the ENI Method and the Capital Method.[8] Under the Capital Method (used by Respondent in calculating the deficiency asserted in the Notice) the tax is computed "at one and one-half mills for each dollar of [a taxpayer's] total business and investment capital, or the portion thereof allocated within the [C]ity. . . ." Code § 11-604.1.E(a)(2).

Business capital is defined as "all assets, other than subsidiary capital, investment capital and stock issued by the taxpayer" (with certain adjustments and exclusions not

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[7] The tax on subsidiary capital is .00075 of each dollar of subsidiary capital allocated within the City. Code § 11-604.1.E(b).

[8] The fourth alternative method used in computing a taxpayer's GCT liability as in effect for the Tax Years is 30 percent of ENI plus salaries and other compensation paid to a taxpayer's elected or appointed officers and greater than five percent shareholders (subject to certain adjustments). Code § 11-604.1.E(a)(3).

relevant herein).[9] Code § 11-602.6(a). In determining the amount of business capital, Code § 11-604.2[10] provides that:

> The amount of . . . business capital shall . . . be determined by taking the average value of the gross assets included therein. . . .

Code § 11-604.2 further provides that in valuing the gross assets included in business capital

> real property and marketable securities shall be valued at fair market value and the value of personal property other than marketable securities shall be the value thereof shown on the books and records of the taxpayer in accordance with [GAAP].

The above language was added to the Code in 1988.[11] Prior to that amendment, Code § 11-604.2 read as follows:

> The amount of . . . business capital shall . . . be determined by taking the average fair market value of the gross assets included therein. . . .

This 1988 amendment to the Code was intended to conform the GCT to comparable amendments made in 1987 to the State Corporate Franchise Tax.[12] The legislative history of both amendments indicates that the above change was intended to modify the "valuation"

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[9] Subsidiary capital is not a component of the Capital Method of computing GCT liability. There is no dispute that Petitioner did not have any investment capital during the Tax Years. Thus, for purposes of computing Petitioner's GCT liability for the Tax Years under the Capital Method, all the assets included in the Capital Method computation are business capital.

[10] Code §11-604.2 also applies in determining the value of the assets included in subsidiary capital and investment capital.

[11] Ch. 525, Laws of 1988 § 15.

[12] Ch. 817, Laws of 1987 § 26. *See* Ch. 525, Laws of 1988, Bill Jacket, Memorandum in Support.

of property.[13] Nothing in the legislative history indicates an intent to alter the nature of the assets included in business capital.

The GCT Rules at 19 RCNY §11-36 provide that "'business capital' means the total average fair market value of all the taxpayer's assets (whether or not shown on its balance sheet) [with certain exclusions]. . . ." Although that rule does not reflect the 1988 amendment to Code §11-604.2 regarding valuation, the comparable State regulation, which was amended subsequent to the 1987 change, similarly states that "*business capital* means the total average value of all the taxpayer's assets (whether or not shown on its balance sheet). . . ." 20 NYCRR § 3-3.3. The State's retention of the parenthetical phrase disregarding the taxpayer's balance sheet suggests that the reference in the 1987 and 1988 amendments to GAAP was not meant to apply in determining which assets are included in business capital.

The issue in this matter is whether the assets to be included in Petitioner's business capital under the Capital Method are Petitioner's interests in the Partnerships under the entity approach or Petitioner's ratable share of the Partnerships' assets under the aggregate approach. The resolution of this issue will dictate which valuation method should apply under Code § 11-604.2. If the assets are the interests in the Partnerships, they will be valued as shown on Petitioner's books and records in accordance with GAAP and if the assets are the ratable portion of the property owned by the Partnerships, the assets will be valued at fair market value.[14]

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[13] Ch. 525, Laws of 1988, Bill Jacket, Budget Report on A11964, "Summary of provisions"; Ch 817, Laws of 1987, Business Tax Reform and Rate Reduction Act of 1987, Governor's Approval Message, August 7, 1987. *See also* TSB-M-87(18)C November 30, 1987.

[14] The Parties have stipulated that the Notice should be cancelled if the assets to be valued are Petitioner's interests in the Partnerships and that the Notice should be sustained if the assets to be valued are Petitioner's ratable portion of the property owned by the Partnerships. Thus, the actual valuation of the

We conclude as did the CALJ that the aggregate approach should be applied to treat Petitioner as owning a ratable share of the Partnerships' property and that those assets should be included in business capital at their fair market value for purposes of the Capital Method of computing Petitioner's GCT liability. Contrary to Petitioner's contention that the Capital Method and the ENI Method of calculating GCT are "fundamentally" different, we conclude, as did the CALJ, that the Capital Method and the ENI Method are not two separate taxes but are merely alternative methods of determining a taxpayer's GCT liability under a single taxing scheme. In Airborne Freight Corp.v. Michael, 94 A.D.2d 669 (1st Dept. 1983), the taxpayer had filed returns under the transportation corporation tax imposed at that time under Subchapter 4 of Chapter 6 of the Code instead of under the GCT imposed under Subchapter 2 of Chapter 6. The court ruled that the filing of the returns under the wrong subchapter nevertheless started the running of the limitations period for assessment of tax stating:

> The [C]ity business tax is composed of a number of separate parts setting forth differing tax rates which are measured on varying bases depending upon the nature of the corporation, but it nonetheless constitutes an integrated corporate tax structure.

Id. at 670.

As Petitioner acknowledges, the aggregate approach has been and continues to be applied for a variety of purposes under the GCT including the computation of ENI, the character of items of income as coming from subsidiary or investment capital, and the calculation of the BAP. The same is true under the comparable State Corporate Franchise Tax. Both the State and City use the aggregate approach for purposes of determining whether a corporation is doing business in the jurisdiction. The GCT Rules provide at 19 RCNY § 11-03(a)(5) that a corporate general partner is subject to the GCT if the "partnership

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assets under either alternative is not at issue.

is doing business, employing capital, owning or leasing property or maintaining an office in [the City]. . . ." In addition the GCT Rules provide at 19 RCNY § 11-06, subject to certain limitations, that "a corporation shall be deemed to be doing business in the City if it owns a limited partnership interest in a partnership that is doing business, employing capital, owning or leasing property, or maintaining an office in the City." The City's use of the aggregate approach for nexus purposes has been upheld by the Court of Appeals. Varrington Corp. v. City of New York Dept. of Finance, 85 N.Y.2d 28 (1995). The State regulations contain comparable provisions regarding nexus for corporate partners.[15]

The starting point for the ENI Method is the taxpayer's federal taxable income subject to various modifications not applicable here. Petitioner does not dispute that for federal income tax purposes, it is required to include its distributive shares of the income, gain or loss from the Partnerships in its federal tax base and that it included those distributive shares in its ENI for the Tax Years.

Taxpayers doing business within and outside the City allocate their business income under the ENI Method and allocate their business capital under the Capital Method using the same three-factor BAP under Code § 11-604.3. Under that formula, a taxpayer is required to separately compute a property factor equal to the value of its property in the City as a percentage of its property everywhere (the "Property Factor") and comparable percentages for its business receipts and its payroll. The percentages are added together and the total is divided by the number of percentages. The Property Factor is computed, pursuant to Code § 11-604.3(a)(1), by "ascertaining the percentage which the average value of the taxpayer's real and tangible personal property, whether owned or rented to it, within the [C]ity during the period covered by its report bears to the average value of all the taxpayer's real and

[15] *See* 20 NYCRR § 1-3.2, paragraphs (5) & (6).

tangible personal property, whether owned or rented to it, wherever situated during such period." Unless the taxpayer elects to use fair market value as the value of all of its real and tangible personal property, "the term 'value of the taxpayer's real and tangible personal property' shall mean the adjusted bases of such properties for federal income tax purposes. . . ."[16] The State regulations provide for the use of the aggregate approach for purposes of computing the BAP of a corporate partner. 20 NYCRR § 4-6.5(a)(1). That regulation expressly provides that a corporate partner must include in its Property Factor its share of the real and personal property of the partnership. 20 NYCRR § 4-6.5(a)(2)(i). *See also* Matter of Gold Fields Mining Corp., TSB-H-85(11)C, New York State Tax Commission (March 19, 1985) (corporate partner allowed to treat a business location of a joint venture as its regular place of business for allocation purposes);[17] Matter of Group W Cable, Inc., FHD 92-428-(GCT) (February 11, 1992). Petitioner included in the Property Factor of its BAP its ratable share of the Partnerships' assets. It would be inconsistent to use the aggregate method in determining the income subject to GCT and the BAP but use the entity approach to determine the business capital allocated by that same BAP.

The State regulations in effect during the Tax Years specifically allowed a corporation whose only nexus to the State was through one or more limited partnerships to elect to be taxed "taking into account only its distributive share of the income, *capital*, gain, loss or deduction of each such limited partnership. . . .[Emphasis added.]" 20 NYCRR § 3-13.1(a).[18] *See also* Department of Finance Audit Division Statement of Audit Procedure AP/GCT - 2

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[16] Petitioner did not elect to use fair market value as the value of all its real and tangible property.

[17] Prior State and City law only permitted taxpayers having a regular place of business outside the jurisdiction to allocate their business income or business capital. *But see infra* Matter of Blenheim Trading Corp.

[18] That section was subsequently renumbered 20 NYCRR § 3-13.5.

(8/27/90) (permitting City auditors to take a similar approach in auditing corporate limited partners.)

Letter Rulings issued by Respondent also have used the aggregate approach to address other issues under the GCT.[19] In FLR(114)-GC-10/84 (October 16, 1984) Respondent ruled that income received by a corporate partner from a partnership exclusively engaged in investment activities can be treated as investment income to the extent the partnership invested in corporate or government securities that would qualify as investment capital if held directly by the partner. In FLR(99)-GC-8/85 (August 22, 1985) Respondent ruled that a corporate partner's share of partnership income attributable to gains from sales of real estate is business income for ENI purposes because real estate is business capital. In that same ruling, Respondent also stated that the corporate partner must include its share of partnership property, receipts and payroll in its BAP and could allocate its business income even if it was not otherwise eligible to allocate income.

Finally, in a decision of the Department's former Hearings Bureau, Matter of Blenheim Trading Corp., FHD 91-409 (GCT) (November 7, 1991), Respondent concluded that the taxpayer corporate partner must include its share of the partnership's assets in capital for its tax year ending on June 30, 1986, but that it was permitted to reduce those assets by its share of the partnership's current liabilities payable within one year.[20] Although the Department Letter Rulings and the decision of the former Hearings Bureau cited above are not binding precedent on this Tribunal, they are consistent with the other authorities cited

[19] Charter section 170.d. does not include Department Letter Rulings as precedent to be followed by the Tribunal.

[20] For the year in question in that case Code § 11-604.2 only permitted business capital to be reduced by current liabilities payable within one year.

above, which reflect a long-standing pattern of using the aggregate approach by the State and City in taxing corporate partners.

Adopting Petitioner's reading of the Code would permit taxpayers to manipulate the value of their capital under the Capital Method simply by moving assets into and out of entities that can be treated as partnerships or corporations merely by "checking a box". Although there is no evidence in the Record that any such manipulation took place in the present case, we note that in a memorandum from Petitioner to the City auditor dated November 5, 2003, attached to Petitioner's May 16, 2007, letter to the Tribunal Commissioners, Petitioner stated that the building at 1345 Sixth Avenue was transferred to a partnership in 1996 while the land under that building was always held by a partnership and that the building at 605 Third Avenue was transferred to a partnership in 1997. There is no indication of the ownership structure for those properties prior to the transfers mentioned.

While Petitioner's GCT liability for the Tax Years is greater under the aggregate approach as a result of valuing its business capital using the fair market value of its ratable share of the Partnerships' real property, the aggregate approach will benefit some taxpayers and disadvantage others. Nevertheless, the aggregate approach is consistent with other aspects of the GCT (*e.g.,* the ENI Method and the calculation of the BAP) and is less subject to manipulation. In comprehensive regulations adopted by the State in 2006 regarding the taxation of corporate partners, the aggregate approach is the general rule and the entity approach is permitted only under limited circumstances.[21]

Petitioner's asserts that the determination of an administrative law judge of the State Tribunal (the "State ALJ") in Matter of Arcade Broadway, New York State Division of Tax

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[21] *See infra* note 24.

Appeals (December 31, 1998), although not binding precedent on either the State Tribunal or this Tribunal, provided guidance to Petitioner in the preparation of the Returns. In Arcade Broadway, the State ALJ concluded that, under an identical State statutory provision (Tax Law §210.2), the taxpayer corporate partners correctly included in business capital their partnership interests as personal property and properly valued those interests at book value under GAAP and not at the fair market value of the corporate partners' shares of the real property held by the partnerships.

While Petitioner acknowledges that the State ALJ determination in Arcade Broadway is not binding precedent on either the State Tribunal or this Tribunal,[22] it contends that in the absence of a pronouncement by Respondent disagreeing with the result in that case, it was entitled to rely on the determination as guidance and to follow it in computing its GCT liability for the Tax Years because to do otherwise "would not have been prudent." Brief for Petitioner's Exception to Determination of Administrative Law Judge, 19.

There is no requirement that Respondent issue a pronouncement when there is a disagreement with a determination of a State Tribunal administrative law judge involving a provision comparable to one contained in the Code. Such a determination cannot become precedential merely because Respondent did not publicly disagree with the result in the matter. Furthermore, in its letter dated May 16, 2007, to the Tribunal Commissioners, Petitioner acknowledged that it was aware that "the City rejected the Arcade Broadway decision" in auditing Petitioner (after Arcade Broadway was issued) with respect to tax years prior to 1997, and that in preparing its initial GCT return for 1999, Petitioner adopted the aggregate approach in valuing its business capital for purposes of the Capital Method. Following the conclusion of a subsequent State audit of Petitioner for tax years prior to 1997

[22] Tax Law § 2010.5; Charter section 170.d. does not include determinations of administrative law judges of the State Tribunal as precedent to be followed by this Tribunal.

in which the State auditors followed Arcade Broadway, Petitioner amended its GCT return for the 1999 Tax Year and recomputed its business capital "using the intangible asset/GAAP valuation approach. . . ."[23] Thus, Petitioner appears to have been aware of Respondent's position both with respect to the application of the aggregate approach and with respect to Arcade Broadway even in the absence of a formal pronouncement, and in fact, initially filed its GCT return for the 1999 Tax Year using the aggregate approach in valuing its business capital under the Capital Method. Moreover, Petitioner now acknowledges that it relied on Arcade Broadway in filing its amended return for the Tax Year 1999 in 2001 after being advised that the City disagreed with that determination. We, therefore, reject Petitioner's argument that it reasonably relied on the State ALJ's determination in Arcade Broadway in preparing any of its Returns and find that to the extent Petitioner did so, it was at its own peril.

Although the State ALJ determination in Arcade Broadway is not binding precedent for either the State Tribunal or this Tribunal, as Petitioner have urged us to adopt the State ALJ's reasoning, we will address it. The State ALJ acknowledged that an aggregate approach applies for the ENI Method and in determining the BAP, but concluded that the tax on the capital base is "fundamentally different in character" from a tax measured on income. The State ALJ did not address the fact that the tax on the capital base uses the same BAP as is used to allocate business income.

The starting point for the State ALJ's analysis is the comparable language in the Tax Law requiring personal property other than marketable securities to be valued using the taxpayer's book value under GAAP for purposes of the State tax on the capital base. Tax Law § 210.2. As we have previously discussed, that language addresses valuation only and

[23] On the amended 1999 Return, Petitioner calculated its GCT liability using the ENI Method.

not the threshold question of which assets are to be included in business capital. Thus, the State ALJ's reliance on various provisions of State law unrelated to taxation that treat a partnership interest as personal property and do not treat a partner as owning an interest in the property of a partnership is misplaced. Those provisions are irrelevant to a determination of what assets are included in business capital of a corporate partner. The numerous instances in which an aggregate approach has been adopted for GCT and State tax purposes discussed above make it clear that the treatment of partnership interests as personal property for non-tax purposes generally has not been applied for tax purposes in the City or State.

The State ALJ also concluded that "there are no provisions in the regulations directing [an aggregate] approach to the valuation of assets under the capital base for corporate partners." As we have previously discussed, 20 NYCRR § 3-13.1 as in effect at that time provided eligible corporate partners with an election to be taxed only on their share of the capital of the partnership. The State ALJ misquotes another State tax regulation in effect at that time, 20 NYCRR § 3-13.2. The correct text of that regulation is as follows:

> Each partnership item of income, capital, gain, loss or deduction has the same source and character in the hands of a partner for article 9-A purposes as it has in its hands for Federal income tax purposes. Where an item is not characterized for Federal income tax purposes, the source and character of the item shall be determined as if such item were realized by the partner directly from the source from which realized by the partnership, or incurred by the partner in the same manner as incurred by the partnership.

The State ALJ determination omits the word "partnership" before the word "item" in the first sentence. The correct text of the regulation makes it clear that partnership items of capital are to have the same source and character in the partner's hands as they have in the partnership's hands. The omission of the word "partnership" in the quoted passage makes the reference to "its hands" in that same sentence unclear. Thus, contrary to the State ALJ's conclusion, we believe that there were State regulations calling for an aggregate approach to the determination of business capital for corporate partners.[24]

Accordingly, the CALJ Determination is affirmed.[25]

Dated: November 30, 2007
New York, New York

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GLENN NEWMAN
President and Commissioner

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ELLEN E. HOFFMAN
Commissioner

[24] On October 17, 2006, the State Department of Taxation and Finance ("DTF") adopted regulations to "set forth both existing and new [DTF] policy regarding the computation of tax . . . for corporations that are partners. The rule largely conforms to the Federal provisions relating to the taxation of partnerships and their partners." Regulatory Impact Statement, "Needs and benefits". The regulations generally require corporate partners to use the aggregate method in calculating their State Corporate Franchise Tax liability unless they cannot obtain the necessary information from the partnership, in which case they are permitted to use an entity approach. Corporate partners are presumed to have access to the necessary partnership information if they meet one or more of a variety of criteria. The City has not adopted comparable rules.

[25] We have considered all other arguments raised by Petitioner and deem them unpersuasive.