STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
STERLING BANCORP	:	DECISION DTA No. 806271
for Redetermination of Deficiencies or for Refund of Franchise Tax on Banking Corporations under Article 32 of the Tax Law for the Years 1980 through 1984.	:	

Petitioner Sterling Bancorp, 540 Madison Avenue, New York, New York 10022, filed an exception to the determination of the Administrative Law Judge issued on December 17, 1992. Petitioner appeared by Hutton & Solomon, Esqs. (Roy F. Hutton and Stephen L. Solomon, Esqs., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Paul A. Lefebvre, Esq., of counsel).

Petitioner filed a brief on exception. The Division of Taxation filed a brief in opposition. Petitioner filed a reply brief. Oral argument, at petitioner's request, was heard on June 3, 1993, which began the six-month period for the issuance of this decision.

Commissioner Dugan delivered the decision of the Tax Appeals Tribunal. Commissioner Koenig concurs.

ISSUES

I. Whether the Division of Tax Appeals has jurisdiction over the matter since the notices of deficiency indicate that they were issued under Article 9-A of the Tax Law, which is applicable to general business corporations, rather than Article 32 of the Tax Law, which is applicable to petitioner as a bank.

II. Whether the doctrine of collateral estoppel was timely raised by the Division of Taxation and, if so, whether petitioner is estopped from litigating the matter before the Division of Tax Appeals.

III. Whether the prior decision of the City of New York, Department of Finance, which was upheld by the appellate courts, is binding upon the present matter under the doctrines of collateral estoppel and/or stare decisis.

IV. Whether the Division of Taxation properly denied petitioner's allocation of a portion of its income for the years at issue to a branch established in Nassau, Bahamas.

V. Whether the Division of Taxation's denial of petitioner's allocation of income to its Nassau, Bahamas branch violated the Commerce Clause of the United States Constitution.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "16" which has been modified. The Administrative Law Judge's findings of fact and the modified finding of fact are set forth below.

On February 7, 1991, the representatives of Sterling Bancorp and the Division of Taxation ("Division") entered into a written stipulation (including Exhibits "A" through "R"), the relevant portions of which are incorporated into Findings of Fact "1" through "8."

1. Sterling Bancorp ("Corp") is a bankholding corporation with its principal office located at 540 Madison Avenue, New York, New York. For the taxable years ended December 31, 1980, December 31, 1981, December 31, 1982, December 31, 1983 and December 31, 1984, Corp filed consolidated New York State franchise tax returns with certain of its wholly-owned subsidiaries, including Sterling National Bank & Trust Company of New York ("SNB").

2. Under date of December 30, 1986, the Division issued statements of audit adjustment and notices of deficiency -- Article 9-A of the Tax Law -- to Corp for the calendar years 1980 through 1984 asserting deficiencies of tax totalling $3,466,634.00, plus interest, for a total due of $5,774,154.00, less a credit allowed of $51,311.00, thereby reducing such total to $5,722,843.00 as follows:

Taxable Year Ended December 31,	Tax	Interest	Total
1980	$ 787,053	$ 753,247	$1,540,300
1981	1,138,594	868,151	2,006,745
1982	896,864	466,867	1,363,731
1982 (Surcharge)	161,428	84,032	245,460
1983	204,840	71,939	276,779
1983 (Surcharge)	34,823	12,230	47,053
1984	207,720	43,636	251,356
1984 (Surcharge)	35,312	7,418	42,730
	$3,466,634	$2,307,520	$5,774,154
Less: Credit			51,311
			$5,722,843

3. SNB is a Federally-chartered bank (national bank) with its principal office located in New York City and, as such, is subject to Title 12 of the United States Code as well as its rules and regulations.

4. On October 18, 1968, SNB filed an application with the Board of Governors of the Federal Reserve System, as required by 12 USC § 601, to open a bank branch in Nassau, Bahamas.

5. On February 20, 1969, the Board of Governors of the Federal Reserve System authorized SNB to open a Nassau, Bahamas bank branch. SNB was duly licensed by the Ministry of Finance, Nassau, Bahamas to open a branch and, on May 26, 1969, SNB notified the Federal Reserve Board of Governors that its banking branch ("NBB") would be opened on June 2, 1969.

6. NBB is a foreign branch as defined in Title 12 of the United States Code and under regulations promulgated by the Federal Reserve System. As such, NBB:

(a) is exempt from the reserve requirements imposed on member banks by Federal Reserve Regulation D;

(b) did not maintain Federal Deposit Insurance on its deposits; and

(c) is not subject to the restrictions imposed on member banks by Federal Reserve Regulation Q relating to the rates of interest payable on its deposits.

7. NBB is located at 50 Shirley Street, Nassau, Bahamas at the offices of World Banking Corporation which it shared with numerous other Bahamian branches of U.S. banks and for which it paid $10,000.00 per year. NBB had no employees of its own. Its books and records were maintained at the offices of SNB in New York. Reports of its banking operations were filed with the Ministry of Finance, Nassau, Bahamas.

8. In the footnotes to the financial statements contained in the Annual Reports issued by Corp, the separate income of NBB for the years ended December 31, 1980, December 31, 1981, December 31, 1982, December 31, 1983 and December 31, 1984 (before taxes), in the respective amounts of $8,813,000.00, $11,700,000.00, $10,357,000.00, $1,734,000.00 and $1,731,000.00, was shown as foreign income.

9. Prior to the issuance of the notices of deficiency, Corp and its consolidated subsidiaries executed consents extending the period of limitation for assessment of tax under Articles 9 (except section 180), 9-A, 9-B, 9-C, 13, 32 and 33 as follows:

Period Extended[1]	Date for Assessment	Consent Executed
YE 12/31/80	12/31/84	5/10/84
YE 12/31/80	6/30/85	10/11/84
YE 12/31/80, 12/31/81	6/30/86	4/16/85
YE 12/31/80, 12/31/81, 12/31/82	12/31/86	5/13/86

10. This case was assigned to the Division's auditor in June 1982. At that time, Corp was also being audited by the Department of Finance of the City of New York ("City"). As a result thereof, the actual audit did not commence until January 1984. The auditor determined that NBB was a "shell" operation since it had no employees there to conduct its business but, instead, employed independent agents. As a result thereof, 100% of the income from NBB was determined to be taxable to New York State.

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[1]Consents were also executed for periods prior to the years at issue. Such consents have not, therefore, been included in this listing.

11. In its application to the Board of Governors of the Federal Reserve System for permission to establish a foreign branch in Nassau, Bahamas, SNB stated that the primary reason for the establishment of the foreign branch was to acquire dollar deposits in the Eurodollar ("Eurodollars" are U.S. dollars owned by foreigners) market. The application stated, in part, as follows:

> "The Voluntary Foreign Credit Restraint Program and the Interest Equalization Tax have provided an incentive for the large banks to open foreign branches to tap the Eurodollar markets. Faced with the necessity of curbing lending to foreigners from home offices, a number of large American banks have come to view the overseas branch as an essential adjunct to their banks, not only for the long-run profits from the branch's operations per se, but also in order to serve adequately the needs of multinational clients (excerpted from 1967 Annual Report of the Comptroller of the Currency).
>
> "It is not feasible for the Bank to emulate the large banks by the opening of a London or other foreign branch because of the near prohibitive costs involved in relation to the capital and earnings of the Bank. A Bahamas branch seems to be the ideal vehicle for this Bank to acquire foreign dollar deposits. The ability to attract domestic deposits both nationally and locally is also restricted in competition with the large banks which have widely scattered facilities and branches, thereby attracting deposits from all sources.
>
> "Approval is sought for the opening of a Bahamas branch of the Bank to be serviced under an agreement with the World Banking Corporation Limited (W.B.C. Ltd.) (Details of arrangement in Exhibit 'C'). It is estimated that the entire net cost of such operation would not exceed $20,000 per year including the annual servicing fee of $15,000 to W.B.C. Ltd. The agreement with W.B.C. Ltd. can be terminated at anytime upon reasonable notice."

12. As previously stated in Finding of Fact "11," the application indicated that the Bahamas branch would be serviced pursuant to an agreement with the World Banking Corporation Limited ("WBC"). Among the pertinent provisions of this agreement were the following:

(a) A small, enclosed, segregated office would be provided to NBB at WBC's building at 50 Shirley Street, Nassau, Bahamas;

(b) NBB's name would be prominently displayed on the outside of the enclosure (painted on the door);

(c) NBB would be furnished, at its own expense, with a desk, two chairs, a file cabinet and such other equipment as might be necessary;

(d) WBC would provide NBB with a branch manager and assistant manager either from its own staff or from qualified local residents outside of the bank (pursuant to a separate contract between NBB and the manager and assistant manager). NBB could be required or, at its discretion, could decide to pay a salary (at least in a token amount) to the manager and assistant manager who, in turn, would endorse such payment over to WBC.

(e) WBC would sublease to NBB such space as might be required by regulations of the Federal Reserve Board to maintain a Nassau branch;

(f) WBC would arrange for installation of a telephone in NBB's office as well as a listing in the Nassau telephone directory. WBC would also arrange for a separate Telex number and cable address for NBB, using WBC Telex equipment if possible;

(g) new loans, deposits and all other banking transactions of NBB would originate at the head office of SNB, thereby requiring no element of decision making by the manager and/or assistant manager in Nassau;

(h) WBC would maintain bookkeeping records for NBB's loans and deposits; and

(i) the annual fee to be charged by WBC for its services and use of its facilities was $15,000.00 (U.S. currency).

13. By letter dated February 20, 1969, the Board of Governors of the Federal Reserve System granted SNB its permission, pursuant to the provisions of section 25 of the Federal Reserve Act, to establish a branch in Nassau, Bahamas and to operate and maintain the branch subject to the provisions of such statute and of Regulation M. This letter stated, in pertinent part, as follows:

"In granting this permission, it is understood that the branch will be used for developing new international business and not as a means of shifting loans or deposits from offices in the United States. It is also understood that there is to be no contact with the local public at the branch, and that its quarters, staff, and bookkeeping may, at least in part, be supplied under contract by another party. In view of the unusual character of this operation, the foregoing permission is granted subject to continuing special observation and review by the Board and after due notice may be withdrawn or modified. The foregoing permission is also granted on the condition that adequate information covering the branch's operations will be maintained at your head office and will be available to the Board and its accredited representatives. The Board should be promptly notified of any modification in the branch's methods of operation, including changes in any contract under which services are supplied to the branch."

14. On October 19, 1978, the Division's Technical Services Bureau issued a memorandum (TSB-M-78[23]C) which provided as follows:

"Subject: Allocation of Entire Net Income of a Banking Corporation

"The following question has been raised concerning Article 32 (Franchise Tax on Banking Corporations) of the Tax Law:

"Question:

"When may a banking corporation which is doing a banking business allocate its entire net income within and without New York State?

"Answer:

"A banking corporation which is doing a banking business may only allocate its entire net income within and without New York State when it is carrying on a full service banking business through its office, branch or agency outside New York State.

"For purposes of Article 32, an office, branch or agency is a permanent place of business which is regularly and systematically maintained, occupied and used by the taxpayer to carry on a full service banking business. Such business must be conducted through its own employees who are regularly in attendance at such place of business during normal business hours. It is not necessary that the office, branch or agency maintained without New York State conduct all the functions of a banking business.

> "For an office, branch or agency to do a full service banking business, it must conduct the following functions on a regular basis:
>
> "1. Approve loans and disburse the funds and
>
> "2. Accept loan repayments
>
> "plus conduct one or more of the other functions of a banking business on a regular basis, such as:
>
> "1. Accept deposits
>
> "2. Pay withdrawals
>
> "3. Cash checks, drafts and other similar items
>
> "4. Issue cashier's checks, treasurer's checks, money orders and other similar items
>
> "5. Buy, sell, pay or collect bills of exchange
>
> "6. Issue letters of credit
>
> "7. Receive money for transmission or transmitting the same by draft, check, cable or otherwise
>
> "8. Exercise fiduciary powers
>
> "A bank which acts as an agent for another bank, is not an office, branch or agency of such bank for New York State purposes."

15. On February 10, 1984, SNB's representative, Roy F. Hutton, Esq., wrote a letter to Edward P. Eustace, Deputy Superintendent of Banks, New York State Banking Department which stated, in part, as follows:

> "Pursuant to Sect. R46-37.2(b) of the Financial Corporation Tax Law of the New York City Finance Corporation Tax Law, the determination of whether a national bank is conducting a banking business is made under both the Federal and State banking laws. As stated above, under the Federal banking law, SNB is deemed to be conducting a banking business outside of the United States at its Nassau branch. Accordingly, we respectfully request that the New York State Department of Banks review the enclosed exhibits for the purpose of determining whether, under the New York State banking laws if applicable to SNB, such bank would be deemed to be conducting a banking business outside of the State of New York at its Nassau branch or conversely whether the banking operations

of such branch would not be deemed part of the banking business conducted by SNB in New York State."

Mr. Eustace's reply, dated February 16, 1984, stated:

"Replying to your letter of February 10, 1984, we confirm that Nassau branch of Sterling National Bank and Trust Company of New York would be considered as a foreign branch for New York State regulatory and supervisory purposes if SNB were a New York State chartered bank.

"In supervising such branch, this Department would follow the same procedures as are applied in the supervision of other branches of state chartered banks located outside the U.S."

We modify finding of fact "16" of the Administrative Law Judge's determination to read as follows:

16. On July 24, 1984, the City issued a decision in the Matter of the Petition of Sterling Bancorp for redetermination of a deficiency of financial corporation tax under Title R of Chapter 46 of the Administrative Code of the City of New York for the years ended December 31, 1979, December 31, 1980 and December 31, 1981. The issue therein was whether the City properly disallowed SNB's allocation of a portion of its net income outside New York City.

In Finding of Fact "7" of this decision, the basis for the deficiencies was set forth, to wit, that the City determined that the Nassau, Bahamas branch of SNB was not a branch where its functions were systematically and regularly carried on within the meaning of financial corporation tax regulation section 2-1(a) and (b). Corp contended that, based upon Administrative Code §§ R46-37.1 and R46-37.2(a) and (b), the only type of business that a corporation subject to the financial corporation tax can do is a banking business as determined by Federal or State banking laws. Therefore, it was Corp's position that a determination as to whether or not SNB's Nassau branch is a branch for purposes of the financial corporation tax must be made by reference to Federal and State banking laws.

Finding of Fact "20" of the City decision indicated that the chief investigator of the City's Enforcement Division visited SNB's Bahamas branch (NBB) in January 1983 (a date subsequent to the audit period at issue in the City matter, but a date within the audit period at issue herein). The findings of the chief investigator, as set forth in Finding of Fact "20," were as follows:

"a) that SNB had a listing in the Nassau, Bahamas telephone directory for premises at 50 Shirley Street, Nassau, Bahamas;

"b) that SNB shared the telephone with some other corporations;

"c) that SNB shared office space at 50 Shirley Street, Nassau, Bahamas, consisting of a room approximately 20 x 40 feet, with approximately forty-six other corporations, most of which appeared to be banks;

"d) that said office contained three to four desks;

"e) that at the time of his visit to said office, which was in midday on a business work day, there was only one female employee on the premises;

"f) that said premises had neither teller windows or any name plates on the desks indicating loan officers; and

"g) that banking hours were not listed on the door to said office."

It should be noted that there is no indication that the Division, in asserting the deficiencies at issue herein, relied on the findings of the City's chief investigator or that the Division made any independent observation of NBB's operation. However, petitioner's vice president for international operations, in a letter to the auditor dated October 28, 1986 stated: "[t]his is to attest to the fact that the Nassau operations in each of the years 1982-84 were of the same nature as the years 1980-81" (Division's Exhibit "E").

The decision held that the City properly disallowed SNB's allocation of a portion of its net income outside New York City. The rationale for this decision was set forth in Conclusions of Law "F" through "L" which stated as follows:

"F. That under section 2-1(b) of these regulations the terms 'Doing Business' and of 'Business Carried On' are defined as follows:

> "'Definitions of "Doing Business" and of "Business Carried On." -- A corporation or association is regarded as "doing business" or "carrying on business" within or without the City when it occupies, has or maintains an office, agency or branch where its functions are systematically and regularly carried on.
>
> "'In order to require an allocation of the income from business carried on within or without New York City, it is not necessary that the branch or agency maintained within or without the City conduct all the functions of the corporation or association. It is sufficient if the branch or office conducts some of the functions which the corporation or association is

> authorized to exercise regularly and with a fair measure of permanency and continuity.'

"G. That references in sections R46-37.2(a) and R46-37.2(b) of the Administrative Code to the Federal and State Banking Laws are merely to determine whether a corporation is subject to the financial corporation tax, pursuant to section R46-37.1(a).

"H. That the determination of whether SNB is doing business or carrying on business at a branch outside the City, so as to enable it to allocate its income pursuant to section R46-37.4 of the Administrative Code, is to be made by reference to regulation section 2-1(b) issued by the Finance Administrator (now the Commissioner of Finance) and not by reference to the Federal and State Banking Laws.

"I. That, although SNB's Nassau facility may qualify as a branch under Federal and State Banking Laws (including the requirements of the Federal Reserve System and Federal Deposit Insurance Corporation (FDIC)), it is not a branch, office or agency where functions are systematically and regularly carried on within the meaning and intent of financial corporation tax regulation section 2-1(b).

"J. That, pursuant to section R46-70.0.5 of the Administrative Code, petitioner had the burden of proof to overcome the deficiency assessment and to show that SNB had the right to allocate a portion of its net income outside the City.

"K. That petitioner did not sustain its burden of proof to show that SNB had the right to allocate a portion of its net income outside the City pursuant to section R46-37.4 of the Administrative Code and regulation sections 2-1(a) and 2-1(b). Petitioner offered no evidence to show that SNB maintained a branch, office or agency outside the City where its functions were systematically and regularly carried on within the meaning of the aforementioned regulations. All transactions of SNB's Nassau branch originate and occur in New York City, including all decisions regarding the investment of funds reported as Nassau branch funds. (See Finding of Fact '16' supra). Moreover, the Nassau branch is not even permitted to deal with the local public. (See Finding of Fact '13' supra).

"L. That SNB's Nassau branch in the Bahamas is a legal device, set up for the sole purpose of enabling it to participate in the Eurodollar market; and wholly lacking the attributes of a bona fide bank branch, office or agency, where its functions are systematically and regularly carried on. (Emphasis added)."

The City's determination was confirmed, without opinion, by the Appellate Division, First Department (Matter of Sterling Bancorp

v. New York City Dept. of Finance, 128 AD2d 1026, 512 NYS2d 609). On July 2, 1987, the Court of Appeals denied Corp's motion for leave to appeal (Matter of Sterling Bancorp v. New York City Dept. of Finance, 70 NY2d 610) and, on July 7, 1987, the Court of Appeals dismissed the appeal (Matter of Sterling Bancorp v. New York City Dept. of Finance, 70 NY2d 692). On March 21, 1988, the United States Supreme Court dismissed an appeal for want of a substantial Federal question (Sterling Bancorp v. New York City Dept. of Finance, 485 US 950, 99 L Ed 2d 409).[2]

OPINION

We deal first with petitioner's assertion that because the notices of deficiency issued by the Division indicated that the deficiencies were asserted pursuant to Article 9-A of the Tax Law instead of Article 32, the Division of Tax Appeals had no jurisdiction over the matter. The Administrative Law Judge rejected this assertion and found that petitioner failed to show that it was in any way prejudiced by the error in the notice, or that such error deprived petitioner of knowledge of the subject matter of the audit. Further, petitioner timely filed petitions protesting the asserted deficiencies. Accordingly, the Administrative Law Judge, relying on Matter of Pepsico, Inc. v. Bouchard (102 AD2d 1000, 477 NYS2d 892), Matter of Tops, Inc. (Tax Appeals Tribunal, November 22, 1989) and Matter of Kadish (Tax Appeals Tribunal, January 12, 1989), reasoned that the assessments should not be cancelled.

On exception, petitioner reiterates its position at hearing that the notices are fatally defective.

The Division characterizes as "spurious" petitioner's assertion that this Tribunal lacks jurisdiction over this matter because of the mistake on the notice (Division's brief, p. 14). The Division asserts that the fact that the assessment was on a form with 9-A in the heading did not mislead petitioner in the least.

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[2]We modified this fact by inserting conclusion of law "F" of the decision in Matter of the Petition of Sterling Bancorp (City of New York Dept. of Fin., July 24, 1984) which sets forth the relevant regulations applied by the hearing officer to the facts in the case.

This issue was dealt with fully and correctly by the Administrative Law Judge and we agree with his determination for the reasons stated therein.

We deal next with petitioner's assertion that the doctrine of collateral estoppel has no application in this case.

The Administrative Law Judge, relying on Capital Tel. Co. v. Pattersonville Tel. Co. (56 NY2d 11, 451 NYS2d 11) and Staatsburg Water Co. v. Staatsburg Fire Dist., (72 NY2d 147, 531 NYS2d 876), found that in order for the doctrine of collateral estoppel to be applicable:

> "(1) that the issue as to which preclusion is sought be identical with that in the prior proceeding; (2) that the issue was necessarily decided in the prior proceeding; and (3) that the litigant who will be held precluded in the present matter had a full and fair opportunity to litigate the issue in the prior proceeding. The court also held that the burden of establishing that the issue was identical and that the issue was necessarily decided in the prior proceeding is on the proponent of preclusion. As to the element of lack of full and fair opportunity to contest the issue, the burden is on the party who opposes the preclusion" (Determination, conclusion of law "C").

Applying these principles to the case at hand, the Administrative Law Judge determined that the City decision was based upon statutes[3] and regulations[4] which were identical to those

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[3]For the years at issue in this proceeding, i.e., taxable years ending December 31, 1980 through December 31, 1984, Tax Law former § 1454(a) provided:

> "[e]ntire net income. -- If the taxpayer's entire net income is derived from business carried on both within and without the state, the portion thereof which is derived from business carried on within the state shall be allocated under rules and regulations prescribed by the tax commission."

For the years ended December 31, 1979, December 31, 1980 and December 31, 1981 (the years applicable to the City determination), Administrative Code of the City of New York former § R46-37.4 provided as follows:

> "[i]f the taxpayer's entire net income is derived from business carried on both within and without the city, the portion thereof which is derived from business carried on within the city shall be allocated under rules and regulations prescribed by the finance administrator."

[4]20 NYCRR former part 35, entitled Apportionment of Income From Sources Within and Without the State, provided, in relevant part, as follows:

> "[s]ection 35.1 Apportionment of Income. (a) The tax is imposed upon that proportion of the net income which is derived from business carried on within the State.
>
> "(b) A corporation or association which maintains an office or place of business within the State, and not elsewhere, is taxable on all of its net income as herein defined. A corporation or association which is doing business or carries on its business through offices maintained both within the State and without the State must apportion its net income as provided in these regulations.
>
> "35.2 Definitions of doing business and of business carried on. (a) A corporation or association is regarded as doing business or carrying on business within or without the State when it occupies, has or maintains an office, agency or branch where its functions are systematically and regularly carried on.
>
> "(b) In order to require an apportionment of the income from business carried on within and without New York State, it is not necessary that the branch or agency maintained without the State, in the case of a domestic corporation or association, or within the State, in the case of a foreign corporation or association, shall necessarily conduct all functions of the banking business of the corporation or association. It is sufficient if the branch conducts some of the functions which the corporation or association is authorized to exercise regularly and with a fair measure of permanency and continuity.
>
> "35.3 Apportionment where business is carried on both within and without the State. (a) A corporation or association doing business or carrying on business both within and without the State which keeps accounts of the income

(continued...)

at issue in the present case and that the issue in this case was identical to the issue decided in the City matter, i.e., the issue of the proper disallowance of SNB's allocation of a portion of its net income outside the City of New York.

The Administrative Law Judge rejected petitioner's contention that it did not have a full and fair opportunity to litigate the matter. The Administrative Law Judge relied on Ryan v. New York Tel. Co. (62 NY2d 494, 478 NYS2d 823), where the Court stated:

> "[a]mong the specific factors to be considered are the nature of the forum and the importance of the claim in the prior litigation, the incentive and initiative to litigate and the actual extent of litigation, the competence and expertise of counsel, the availability of new evidence, the differences in the applicable law and the foreseeability of future litigation" (Ryan v. New York Tel. Co., supra, 478 NYS2d 823, 827).

Applying these principles to the instant case, the Administrative Law Judge determined that:

> "[i]n the prior proceeding, the amount at issue (after a reduction in the deficiency) was $1,264,429.00, plus interest, a not insignificant sum of money. Petitioner's representatives, in the

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[4](...continued)
of each branch or agency which in the opinion of the Tax Commission actually reflect the net income from business carried on within the State of each branch, should report as its net income subject to tax, the income derived from the branches or agencies maintained within the State. In all cases, however, a report will be required of the gross and net income of the corporation or association from all business carried on within and without New York State."

The applicable New York City regulation (referred to in the City decision) was section 2-1(b) which provided as follows:

> "[d]efinitions of 'Doing Business' and of 'Business Carried On'. -- A corporation or association is regarded as 'doing business' or 'carrying on business' within or without the City when it occupies, has or maintains an office, agency or branch where its functions are systematically and regularly carried on.
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> "In order to require an allocation of the income from business carried on within or without New York City, it is not necessary that the branch or agency maintained within or without the City conduct all the functions of the corporation or association. It is sufficient if the branch or office conducts some of the functions which the corporation or association is authorized to exercise regularly and with a fair measure of permanency and continuity."

> proceeding before the City and on appeal, were the same representatives as in the present matter. At the hearing in the present matter, no new evidence was presented. As previously indicated, there is little or no difference between the statutes and regulations at issue in both matters. The record on review which was considered by the Appellate Division in support of petitioner's petition, pursuant to Article 78 of the Civil Practice Law and Rules, for a judgment annulling the City's determination consisted of over 1,000 pages. It cannot be found, therefore, that petitioner did not have a full and fair opportunity to litigate the issue in the prior proceeding. Accordingly, it is hereby found and determined that the doctrine of collateral estoppel is applicable herein and that petitioner is barred from relitigating the issue of whether its allocation of a portion of its income to a branch located in Nassau, Bahamas was proper" (Determination, conclusion of law "E").

On exception, petitioner asserts that the principle of collateral estoppel is inapplicable in this matter since "the decision in the Hearing of the Finance Commissioner of the City of New York, was not rendered after a fair and impartial trial of the issues" (Petitioner's brief, p. 3). Petitioner asserts that the City decision is, in effect, made by the Finance Commissioner since any decision of a hearing officer must be approved and accepted by the Commissioner. "Certainly it cannot be said that such decision was unbiased when the Hearing Officer's authority is so circumscribed" (Petitioner's brief, p. 4)

As specific evidence of the unfairness, petitioner points to the fact that the hearing officer for the City granted the City's objection to strike the testimony of a representative of the New York State Banking Department on the grounds that it was immaterial and irrelevant. "The lack of independence of the Hearing Officer is demonstrated by the fact that he granted this objection when there was no jury at a Formal Hearing and striking such testimony from the record makes it unavailable for subsequent court review. The failure to permit a key witness to testify is, in itself, evidence that the petitioner was not given a full and fair opportunity to contest the issue" (Petitioner's brief, p. 5).

Petitioner also asserts that:

> "the principle of collateral estoppel is also inapplicable because it does not apply to an unmixed question of law. [cite omitted]

> "The issue involved herein is solely one of law. There are no factual issues or mixed issues of fact and law. The [Division] denied the petitioner's allocation on the basis that the activities of the Nassau branch were conducted by independent agents rather than by its own employees. Thus, the issue is whether a bank is required by the Tax Law to have its own employees conduct its activities in order to be permitted an allocation for purposes of the franchise tax imposed on banking corporations. This is solely a question of law" (Petitioner's brief, pp. 5 and 6).

In essence, petitioner asserts that the Division's regulations, which require that bank functions be "systematically and regularly carried on" are inconsistent with the statute and, thus, invalid.

On exception, the Division asserts that the issue presented in this case has already been decided by the courts (Matter of Sterling Bancorp v. New York City Dept. of Fin., 128 AD2d 1026, 512 NYS2d 609, appeal dismissed 70 NY2d 692, 518 NYS2d 1027, appeal dismissed 485 US 950). The Division asserts that the record in the prior proceeding (Exhibit "A") shows clearly that the issue is the same as that presented here and "[f]urthermore . . . the record and the petitioners' [sic] brief [show] that the provisions of the Administrative Code of the City of New York and its regulations parallel those of the Tax Law, as do the arguments the petitioner made then and is making now" (Division's brief, p. 3).

We reverse the determination of the Administrative Law Judge and conclude that the doctrine of collateral estoppel is not applicable.

It is not clear from the record in this case that the two basic requirements of collateral estoppel have been satisfied: "(1) the identicality of an issue necessarily decided in the prior action with one which is decisive of the present action, and (2) that there was a full and fair opportunity to contest the issue in the prior action" (Matter of Halyalkar v. Board of Regents, 72 NY2d 261, 532 NYS2d 85, 87). "For a question to have been actually litigated so as to satisfy the identicality requirement . . . it must have been properly raised by the pleadings or otherwise placed in issue and actually determined in the prior proceeding" (see, Matter of Halyalkar v.

Board of Regents, supra, 532 NYS2d 85, 89).[5] In the instant case, petitioner challenges the validity of the Division's regulations and TSB-M-78(23)C. Clearly, the validity of the Division's regulations was not actually litigated in the City case; thus, there is no identity of issue between the issue in the City case and the issue here.[6]

In view of the fact that estoppel is an elastic doctrine, based on general notions of fairness involving a practical inquiry into the realities of litigation (Matter of Halyalkar v. Board of Regents, supra), the principles of which are not to be applied in a mechanical fashion (Staatsburg Water Co. v. Staatsburg Fire Dist., supra) and that the use of the doctrine "offensively" by a nonparty in the prior litigation (here, the Division) in some cases raises legitimate concerns about the fairness of its application (Matter of Halyalkar v. Board of Regents, supra), we conclude that because the validity of the Division's regulations was not challenged in the City case, the doctrine is not applicable in this case. Accordingly, we address the merits of petitioner's argument.

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[5]The portions of the City decision dealing with petitioner's challenges to the City regulations are: Finding of fact "8": "[i]t is the petitioner's contention that, based upon sections R46-37.1, R46-37.2(a) and R46-37.2(b) of the Administrative Code, the only type of business that a corporation subject to the financial corporation tax can do is a banking business as determined under the Federal or State Banking Laws. Therefore, it is contended that the determination whether or not [petitioner's] Nassau branch is a branch for purposes of the the financial corporation tax must be made by reference to the Federal and State Banking Laws"; Finding of Fact "22": it is petitioner's contention that the City Finance Administrator "could only issue rules and regulations with respect to the allocation of income derived from business carried on within the City and, therefore, he had no authority to issue rules and regulations concerning the allocation of income which petitioner claims is derived from business activities carried on by [petitioner] outside the City"; and Conclusion of Law "N": "[t]hat petitioner's contention that the Finance Administrator . . . had no legislative authority to issue rules and regulations as to the allocation of the income of [petitioner's] Nassau, Bahamas branch is without merit since it has been determined that all activity from which the income in question was derived took place within New York City" (Matter of the Petition of Sterling Bancorp, City of New York Dept. of Fin., July 24, 1984).

[6]Nor do we find the related doctrine of stare decisis, referred to by both parties at hearing, to be applicable. In short, while petitioner raised the issue of the validity of the City regulations at hearing [it is not at all clear from the record whether the City hearing officer had the authority to rule on the validity of the regulation (cf., Tax Law § 2006[7] which provides explicit authority to this Tribunal to rule on the validity of regulations adopted by the State Commissioner of Taxation and Finance). Moreover, while the issue was raised before the Appellate Division (Division's Exhibit "A," Appellate Division brief, p. 16)], the Appellate Division's affirmance without opinion provides no insight on that Court's thinking on the issue.

Petitioner asserts that since the term "banking business is defined in section 1452(b) . . . of the Tax Law as such business as a national banking association is created or organized to do under the Banking Laws of the United States. . . . the term 'business' for purpose of Article 32 of the Tax Law, must mean 'banking business' as determined by the Banking Laws since this is the only business that a banking corporation can do" (Petitioner's brief, p. 13). The essence of petitioner's argument is that the Division's regulations, which require that the bank functions be "systematically and regularly carried on," are inconsistent with the statute and, thus, invalid.

Petitioner also asserts that it was in compliance with the statute and the (Division's) regulations which merely require that the branch carry on some, but not all, of the functions of the banking business. Petitioner, referring to the Division's TSB-M-78(23)C, also asserts that the denial of allocation "on the basis that [the Nassau] branch was a 'shell' operation since it had no employees to conduct its business but, instead, employed independent agents . . . [is based on a] requirement . . . not found in the Tax Law or regulations" (Petitioner's brief, p. 7). Petitioner states specifically that:

> "[t]here is no mention of a requirement that such branch conduct all of the functions of its banking business with its own employees. The petitioner's subsidiary had a branch outside of New York which carried on a banking business. These facts are undisputed. Its operations were conducted under a banking license issued by Nassau, Bahamas and it was subject to the supervision and control thereof. Thus, under the Tax Law and [the Division's] regulations, the petitioner's subsidiary is entitled to allocate the income of its Nassau branch. The [Division] must follow its own regulations" (Petitioner's brief, pp. 8 and 9).

The Division asserts that its regulations and the TSB-M-78(23)C are a valid exercise of its rule-making authority.

The Division asserts that the Division properly determined that petitioner's Nassau operation was a "shell" and not a true branch which would allow the allocation of income. The Division summarizes its position by stating that:

> "[i]t should be noted that no decisions were made at Sterlings' shell facility and the shell facility books and records were

> located in New York. The bank had no employees of its own at the shell facility and its agents there apparently performed what were essentially clerical functions. The Articles 9-B and 9-C regulation said that a bank is doing business or carrying on business without New York if it has an office, branch or agency where its functions are systematically and regularly carried on. During the administrative proceeding before the New York City Department of Finance Sterling Bancorp was not able to show that its shell facility was systematically and regularly carrying on the functions of a bank. Thus, Sterling Bancorp may not allocate and the Division properly held one hundred percent of its income and expenses to be attributable to New York" (Division's brief, p. 13).

We reject petitioner's assertion that the Division's regulations are inconsistent with the statute.

The statute clearly provides the Division with the authority to promulgate rules and regulations concerning allocation of entire net income (former Tax Law § 1454). Pursuant to this authority, and in the absence of a statutory definition, the regulations define the phrase "business carried on within the state" to mean that the bank:

> "has or maintains . . . [a] branch where its functions are systematically and regularly carried on.
>
> * * *
>
> "It is sufficient if the branch conducts some of the functions which the corporation is authorized to exercise regularly and with a fair measure of permanency and continuity" (former 20 NYCRR 35.2[a][b], emphasis added).

Administrative regulations which merely fill in the details of broad legislation describing the overall policy to be implemented are not inconsistent with the statute nor do they constitute an exercise of rulemaking power in excess of the statutory grant of power to an agency (Matter of Mercy Hosp. of Watertown v. New York State Dept. of Social Servs., 79 NY2d 197, 581 NYS2d 628). The pattern of the legislation here is quite clear. The Legislature, through specific statutory definitions determined which entities were taxable.[7] The allocation of entire net income

[7]Specifically, the tax was imposed on every "banking corporation" for the privilege of "exercising its franchise or doing business in this state" (former Tax Law § 1451[a]). "Banking corporation" was defined, in relevant part, as (continued...)

derived from business carried on both within and without the State is a separate and distinct aspect of the statute. Specifically, the Legislature provided that "the portion [of entire net income] . . . derived from business carried on within the state shall be allocated under rules and regulations prescribed by the [Division]" (former Tax Law § 1454). In short, the Legislature delegated to the Division the task of establishing criteria to determine whether entire net income is derived from business carried on within and without the State. We find nothing in the requirement of the Division's regulations that a bank branch "systematically and regularly" carry on the functions of the bank in order to allocate entire net income, which renders it inconsistent with the statute or in excess of the rulemaking power delegated to the Division (cf., Matter of Boreali v. Axelrod, 71 NY2d 1, 523 NYS2d 464). The Division has merely established criteria to determine whether, in fact, a bank is carrying on business within and without the State. Accordingly, we conclude that the Division's regulations are a valid exercise of the rulemaking power delegated to it by the Legislature.

We reject petitioner's assertion that it meets the requirements of the regulations in that it has a branch in Nassau. The crux of petitioner's position is that the mere establishment of the Nassau branch means that petitioner "carries on any business" in Nassau, as required by section 1454(a) and the Division's regulations. We cannot agree.

Petitioner has not shown that it "regularly and systematically" carried on business in compliance with the Division's regulations.

Application of the regulations to the uncontroverted facts shows that: all of the transactions of the Nassau branch originated and occurred in New York City; the records of the branch were kept in New York City; all decisions regarding investment of the funds reported as

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[7](...continued)
any corporation organized under the laws of New York and authorized to do a "banking business, or which is doing a banking business" (former Tax Law § 1452[a][1]). It also included corporations organized under the laws of any other state or country, or under the authority of the United States "doing a banking business" (former Tax Law §§ 1452[a][2][3], 1453[b]).

Nassau branch funds were made by the investment committee located in New York City; and the assets attributed to the Nassau branch were all deposited in time deposits in foreign banks, the foreign branches of domestic banks or the International Banking Facilities of other banks. In short, application of the regulations shows that the business was carried on in New York, not in Nassau.[8]

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Sterling Bancorp is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Sterling Bancorp is denied; and
4. The notices of deficiency issued on December 30, 1986 are sustained.

DATED: Troy, New York
November 18, 1993

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner

[8]In view of the fact that petitioner has failed to prove that it complied with the Division's regulations, we do not have to address the validity of TSB-M-78(23)C.