STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
BANKERS TRUST NEW YORK CORPORATION	:	DECISION DTA No. 811316
for Redetermination of a Deficiency or for Refund of Franchise Tax on Banking Corporations under Article 32 of the Tax Law for the Years 1984 through 1987.	:	

Petitioner Bankers Trust New York Corporation, c/o Corporate Tax Department, P.O. Box 1703, Wall Street Station, New York, New York 10268, filed an exception to the determination of the Administrative Law Judge issued on November 3, 1994. Petitioner appeared by Hutton & Solomon, Esqs. (Stephen L. Solomon and Kenneth I. Moore, Esqs., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (John O. Michaelson, Esq., of counsel).

Petitioner filed a brief in support of its exception. The Division of Taxation filed a brief in opposition and petitioner filed a reply brief. Oral argument was heard on September 14, 1995, which date began the six-month period for the issuance of this decision.

Commissioner DeWitt delivered the decision of the Tax Appeals Tribunal. Commissioners Dugan and Koenig concur.

ISSUES

I. Whether bonds of the New York City Municipal Water Finance Authority and interest earned thereon are excluded from the measurement of a bondholder's franchise tax liability.

II. If petitioner prevails on its claim that interest on bonds of the New York City Municipal Water Finance Authority (and, consequently, interest on Federal obligations) should not be included in the measurement of petitioner's franchise tax liability, may the Division of Taxation exclude expenses indirectly attributable to interest income from Federal obligations based on a

ratio of petitioner's Federal interest income to total income applied to petitioner's total interest expenses and total deductions.

III. Whether the Tax Appeals Tribunal has jurisdiction to determine if a violation of the secrecy provisions of Tax Law § 1467 occurred and, if so, whether such secrecy provisions were violated by the Division of Taxation.

IV. Whether petitioner properly submitted its complete Federal tax returns after the close of the hearing.

V. Whether petitioner may deduct 17% of the interest received from indirect subsidiaries in computing its entire net income.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "13," "14" and "17" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

A Registration Statement (Form S-3), which petitioner, Bankers Trust New York Corporation, filed with the Securities and Exchange Commission on October 29, 1987, included the following description of petitioner and its banking operations:

> "The Corporation is a bank holding company, incorporated under the laws of the State of New York in 1965. The Corporation's principal subsidiary is Bankers Trust Company ('Bankers'). At June 30, 1987, the Corporation had consolidated assets of $54.7 billion, of which Bankers accounted for approximately 91%.
>
> "Since 1980, the Corporation has disposed of its upstate New York banking operations, most of the Metropolitan New York branch office network of Bankers and its credit card operations in order to concentrate its financial and managerial resources on selected wholesale markets. In so concentrating its resources, under the name of merchant banking the Corporation has combined the on-balance-sheet capability and service breadth of a commercial bank with the intermediary skills and entrepreneurial spirit of an investment bank.
>
> "Bankers, founded in 1903, was the sixth largest among commercial banks in New York City and the seventh largest in the United States based on total assets of $54 billion at December 31, 1986.

"Bankers' worldwide resources are concentrated on merchant banking for corporations, governments, financial institutions and high-net-worth individuals. The core business organizations of Bankers are Financial Services and PROFITCo. Financial Services consists of Corporate Finance, Global Markets and Investment Banking. PROFITCo. is comprised of Fiduciary and Securities Services, Investment Management, Private Clients Banking and Global Operating and Information Services.

* * *

"The Global Markets Function has responsibility for the business lines which are involved with markets, risk management and the funding of the Corporation worldwide. These include primary dealer operations in the securities of the U.S. Government and its agencies . . . .

* * *

"The Corporation is a legal entity separate and distinct from its subsidiaries, including Bankers. There are various legal limitations governing the extent to which the Corporation's banking subsidiaries may extend credit, pay dividends or otherwise supply funds to the Corporation or certain of its other subsidiaries. The rights of the Corporation to participate in any distribution of assets of any subsidiary upon its liquidation or reorganization or otherwise (and thus the ability of holders of the Common Stock to benefit indirectly from such distribution) are subject to the rights of those with prior claims on that subsidiary, except to the extent that the Corporation may itself be a creditor of that subsidiary . . ." (emphasis added).

Petitioner filed combined[1] New York State franchise tax returns for banking corporations (Forms CT-32) for each of the years at issue including interest from Federal obligations in the measurement of its entire net income as follows:

Year	Interest from Federal Obligations Reported
1984	$102,325,337.00
1985	140,743,980.00
1986	125,156,443.00
1987	76,527,382.00

[1]The complex returns of petitioner, a bank holding company, covered over 60 affiliated companies.

For the years 1985 through 1987, petitioner deducted 22.5% of the interest from Federal obligations which it held for investment pursuant to Tax Law § 1453(e)(12)[2] as follows:

Year	Amount of Deduction
1985	$2,153,790.00
1986	4,347,005.00
1987	6,435,674.00

For the years 1985 through 1987, in calculating its taxable assets, petitioner included the value of its Federal obligations as follows:

Year	Value of Federal Obligations Included in Taxable Assets
1985	$1,664,211,000.00
1986	2,015,174,000.00
1987	1,203,478,000.00

The parties agreed that this matter will serve as "one lead case", in the words of attorney Moore in his letter of February 2, 1994 to Daniel J. Ranalli, Assistant Chief Administrative Law Judge, with regard to the issue concerning the exclusion of United States obligations and the interest thereon in computation of entire net income and capital. The following ten matters were placed on hold pending resolution of this matter:

Astoria Federal Savings and Loan	DTA# 811306
Long Island Savings Bank FSB	DTA# 811792
Sterling Bancorp and Subsidiaries	DTA# 811793
Sunrise Federal Savings and Loan	DTA# 811552
Bank of New York Co.	DTA# 811771
Bank of New York Co. (Irving Trust Co.)	DTA# 811772
Gouverneur Savings and Loan	DTA# 811773
Hamilton Savings and Loan	DTA# 811774
Hudson Valley Holding Corp.	DTA# 811775
Donaldson Lufkin and Jenrette	DTA# 812167

[2]Tax Law § 1453(e)(12) was added by Laws of 1985 (ch 298, § 18, eff July 10, 1985, retroactive to taxable years beginning on or after January 1, 1985). It provides a deduction in determining entire net income for:

> "twenty-two and one-half percent of interest income on obligations of New York state, or of any political subdivision thereof, or of the United States, other than obligations held for resale in connection with regular trading activities [i.e., for obligations held for investment]" (emphasis added).

Petitioner filed four timely claims for refund of franchise tax on banking corporations on forms CT-8, Claim for Credit or Refund of Corporation Tax Paid, as follows:

Date of Signing of Refund Claim	Year at Issue	Amount of Refund Claim	Basis Stated for Refund Claim on Form
October 12, 1990	1984	$ 3,136,413.00	(1) Tax impermissibly discriminated against obligations of the United States Government and the interest on such obligations so that such obligations and the interest thereon should be excluded from the measure of the tax.
December 15, 1990	1985	$ 38,895.00	(1) Same basis as "1" for the 1984 year; (2) Subtraction correction regarding the 22½% deduction for interest earned on New York State municipal securities; and (3) Inclusion of a subtraction for 17% of the interest earned on subsidiary capital.
December 15, 1990	1986	$11,146,380.00	(1) Same basis as "1" for the 1984 and 1985 years plus (2) Subtraction correction regarding the 22½% deduction for interest earned on New York State municipal securities.
March 7, 1991	1987	$12,759,828.00	(1) Same basis as "1" for all of the earlier years.

By a letter dated October 31, 1990, the Division of Taxation ("Division") denied petitioner's refund claim for 1984. No explanation for the denial was provided in this letter.

By a letter dated March 8, 1991, the Division denied petitioner's refund claims for 1985 and 1986. This letter referenced the claims dated December 15, 1990 described in Finding of Fact "4". It also referenced a refund claim dated November 19, 1990 for 1985, 1986 and 1987

with reference to an issue described as "IBF eligible net income (loophole)". (A copy of the refund claim dated November 19, 1990 was not made a part of the record.) The following explanation for the denial was provided:

> "You [sic] claims are being respectfully denied for the following reasons:
>
> "(1) As you know, we do not recognize the loophole issue . . . .
>
> "(2) Under Tax Law Section 1453(e)(11)(i), a deduction for 17% of interest received from subsidiary capital is allowed. This deduction is only allowed for interest from 1st tier subs. Since the interest you are claiming is from other than 1st tier subs, the deduction will not be allowed.
>
> "Tax Law Section 1453(b)(1) requires the addback of any income exempt from Federal taxable income. Interest income from U.S. Government obligations must be added back to FTI each year.
>
> * * *
>
> ". . . It is not clear in your claim what [the amounts claimed for the 22.5% deduction and corrections to IBF eligible net income] are from, or if they have already been addressed on audit."

By a letter dated January 29, 1992, the Division denied petitioner's refund claim for 1987 and provided the following explanation:

> "[T]he interest on bonds issued pursuant to Title 8A of Article 5 of the Public Authorities Law is included in entire net income. Therefore, New York does not discriminate in its treatment of obligations issued by the State or its local municipalities and your refund claim for $3,786,914.00[3] . . . is respectfully denied."

Included in petitioner's Exhibit "5", an affidavit dated April 9, 1993 of William F. Collins, Deputy Commissioner and Counsel of the Department of Taxation and Finance, is a photocopy of a letter dated October 2, 1990 on the letterhead of petitioner's attorneys to an

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[3] As noted in Finding of Fact "4," petitioner's refund claim for 1987 was for $12,759,828.00. This variation was not explained, although marked into evidence as petitioner's Exhibit "2" was a computation of revised tax which the parties agreed "would be an accurate reflection of . . . Petitioner's claim for refund attributable to the U.S. obligations [aside from the attributions of expenses as further discussed in Finding of Fact "10"]." Exhibit "2" shows amounts claimed for refund attributable to U.S. obligations as $4,004,133.00 for 1987, $6,413,829.00 for 1986, $38,895.00 for 1985, and $3,136,413.00 for 1984.

officer of the New York League of Savings Institutions. This letter solicited "savings institutions which included the income or capital attributable to U.S. obligations in the computation of the State or City franchise taxes" to file refund claims with the attorneys' assistance because "in recent years the City and State taxes have become discriminatory, since numerous New York State and City obligations are treated more favorably than U.S. government obligations." According to Mr. Collins' affidavit, "the Department became aware of the differences in interpretation of certain sections of the Public Authorities Law . . . [as] the result of [such] correspondence from the law firm of Hutton & Solomon to various banks . . . ." Consequently, the Division's Technical Services Bureau issued a memorandum dated December 18, 1990, TSB-M-90-(14)C, which noted that the bonds or the interest on the bonds issued under 1984 legislation known as Title 8-A of Article 5 of the Public Authorities Law, "The New York State Local Water and Sewer Authority Act", were not exempt from franchise taxes. The Division's memorandum interpreted the 1984 legislation, Public Authorities Law § 1196-1(3),[4] to mean the exemption from franchise taxes "refers to and modifies the exemption from taxation of activities of the Authority but not the bonds or the interest from the bonds of the Authority."

Deputy Commissioner Collins testified that he personally researched the intent behind the 1984 legislation as a result of his:

> "[trying] to figure out where this argument may have sprung from that Mr. Solomon was spreading . . . . Several bank people, as I recall, called the Commissioner and asked what was the Commissioner's intention here. Were they going to be embarrassed by not joining the lawsuit or such a lawsuit" (tr., p. 117).

Mr. Collins discovered "no intention [with the 1984 legislation] to change the breadth of the initial exemption" for bonds issued by public authorities (tr., p. 119).

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[4]The same language is found in the original versions of the specific sections of the Public Authorities Law relating to the following local authorities: Green Island Power Authority, § 1020-m; New York City Municipal Water Finance Authority, § 1045-u; Buffalo Municipal Water Finance Authority, § 1048-u; Albany Municipal Water Finance Authority, § 1115-t; Town of Clifton Park Water Authority, § 1120-n; Water Authority of Great Neck North, § 1197-m; Water Authority of Western Nassau County, § 1198-n; Rensselaer County Water and Sewer Authority, § 1199-n; Wayne County Water Authority, § 1199-nn; Orange County Water Authority, § 1199-oo; Saratoga County Water Authority, § 1199-nnn; Greater Utica Area Water Finance Authority, § 1226-m.

Nonetheless, Deputy Commissioner Collins testified:

> "We decided collectively in the Executive Branch, [i.e.] Governor's Counsel, Division of Budget and we in the Department [of Taxation and Finance], that it would be desirable to correct the language of those provisions so that the intent would be absolutely clear in the nature of a technical correction" (tr., p. 134).

As a result, in 1991, the statutory language at issue was amended to clearly provide that the bonds (and interest income thereon) of the New York City Municipal Water Finance Authority and similar entities were not exempt from franchise taxes.

Commencing in or about November 1985, bonds were issued by the following New York public authorities pursuant to the statutory language at issue as follows:

New York City Municipal Water Finance Authority

Series:	Amount of Issue:	Dated:
1986-A	$ 200,000,000.00	11/1/85
1986-B	200,000,000.00	4/1/86
1987-A	388,650,000.00	1/15/87
1987-B	160,278,231.45	6/1/87
1988-A	244,915,000.00	10/1 or 10/14/87
1988-B	245,000,454.95	3/1 and 3/30/88
1989-A	275,001,169.50	11/3/88
1989-B	288,057,995.20	3/28/89
1990-A	281,474,424.50	12/13/89
1991-A	285,000,004.00	8/16/90
1991-C	354,610,000.00	2/28 or 3/7/91
1992-C	200,000,000.00	6/25/92
1993-A	1,040,704,592.35	8/13/92
1993-B	125,000,000.00	10/15/92
1993-C	100,000.000.00	10/15/92

Albany Municipal Water Finance Authority

Series:	Amount of Issue:	Dated:
1988-A	$ 46,700,000.00	1/1/88

Great Neck North Water Authority

Series:	Amount of Issue:	Dated:
1989-A	$ 18,170,000.00	12/1/89

Domenick Sciortino, Director of the Division's Corporation Tax Audit Bureau, testified that approximately 800 banks file franchise tax returns and that, over a three-year cycle, virtually all of them are audited (tr., p. 78). His testimony also confirmed the following statement in his affidavit of April 1993 (Division's Ex. "D" [which did not specify a particular day in April]):

> "As the Director of the Corporation Tax Audit Bureau I am intimately aware of the tax policies of the Department. It is the regular business practice of the Department to treat all income from federal and state obligations equally. The income from both types of obligations are subject equally to New York State income or franchise tax. There has never been any policy of the Department to exclude the income from any state obligation, nor is there such a policy at the present time."

Expenses Indirectly Attributable to Interest Income

The Division contended that if petitioner is permitted to exclude (i) interest from Federal obligations in the measurement of its entire net income and (ii) the value of Federal obligations in the measurement of its taxable assets, expenses (including interest expense and deductions) indirectly attributable to interest income from such Federal obligations should also be excluded. John Verde, the Division's auditor, testified concerning his methodology for calculating expenses indirectly attributable to interest income. He used a ratio consisting of petitioner's interest income from Federal obligations divided by petitioner's total income. For example, he computed a ratio of 1.6789% for 1984 based upon interest income from Federal obligations for 1984 of $102,242,793.00 divided by total income for such year of $6,089,704,058.00. This ratio of 1.6789% was then applied to interest expense of $4,885,607,135.00 and total deductions of $5,917,354,572.00 to calculate interest expense attributable and deductions attributable of $82,026,666.00 and $99,349,140.00, respectively. According to the auditor, such amounts should be disallowed as deductions if interest income from Federal obligations is excluded. Similar calculations were performed for each of the other three years at issue and were summarized in the Division's Exhibit "C".

Harry Montgomery, a vice-president of petitioner and the managing director of its tax department, testified that out of petitioner's 8,600 employees in the United States during 1985, fewer than 10 people dealt with investments in Federal obligations. Furthermore, Mr. Montgomery testified that petitioner did not incur interest specifically to purchase Federal obligations:

> "Most of our interest expense is as a result of the bank's interest expenses, primarily, a result of deposits, period" (tr., p. 187).

We modify finding of fact "13 of the Administrative Law Judge's determination to read as follows:

Interest from Indirect Subsidiaries

Petitioner claims that it is entitled to a deduction for 17% of the interest income earned from the following subsidiaries, as noted in its Exhibit "12", for each of the years 1985 through 1987[5] as follows:

Name of Subsidiary	Interest Received 1985	1986	1987
Bankers Trust Holding (U.K.) Ltd.	$ 64,769,000.00	$109,372,000.00	$ 89,140,000.00
Bankers Trust (France) S.A.	6,932,000.00	20,276,000.00	34,212,000.00
B T Asia Limited	27,499,000.00	24,979,000.00	11,542,000.00
Bankers Trust GmbH	28,920,000.00	49,261,000.00	55,988,000.00
B.T. Australia Limited	2,954,000.00	4,331,000.00	19,194,000.00
Bankers Trust International (Asia) Ltd.	371,000.00	3,781,000.00	2,693,000.00
Malta Properties Ltd.	579,000.00	2,306,000.00	4,471,000.00
BT Servicios Financieros S.A.	-0-	-0-	897,000.00
Bankers Trust A.G.	4,550,000.00	1,608,000.00	1,082,000.00
Bankers Trust Finanziaria S.p.A.	332,000.00	379,000.00	150,000.00
Bankers Trust Company International	559,000.00	282,000.00	54,000.00
BT Bank of Canada	-0-	-0-	5,000.00
BT Foreign Investment Corp.	1,066.00	-0-	-0-
Total Interest Received	$138,531,000.00	$216,575,000.00	$219,428,000.00

Although Mr. Montgomery testified that the amounts shown as interest received came from petitioner's books and records, such books and records were not "brought" to the hearing (tr., p. 216). Further, contrary to petitioner's claim, the only year for which a refund was requested based on a deduction for 17% of the interest income earned from subsidiaries was 1985. Petitioner's claim for refund for that year indicates that petitioner failed to subtract the claimed amount in the computation of its entire net income. Although the Division, on audit, disallowed all or most of the amount claimed as a deduction for 17% of subsidiary interest income by petitioner for 1986 and 1987, the results of that audit are not the subject of this proceeding. (A copy of the audit report is annexed as Exhibit "11" to the stipulation between the parties dated April 16, 1993.) In this proceeding, petitioner is only challenging the denial of its claims for refund, which claims were filed and denials issued by the Division prior to the completion of the audit. Therefore, the issue for resolution in this proceeding is whether petitioner has

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[5] Tax Law § 1453(e)(11)(i), which allows a deduction for 17% of the interest received from subsidiary capital, was enacted by Laws of 1985 (ch 298, § 18, eff July 10, 1985, retroactive to taxable years beginning on or after January 1, 1985).

demonstrated its entitlement to the claimed deduction for 1985 only.[6]

We modify finding of fact "14" of the Administrative Law Judge's determination to read as follows:

> Mr. Montgomery testified that "[t]here's no question in my mind" that Bankers Trust Company, petitioner's principal subsidiary as noted in Finding of Fact "1", owns and controls the subsidiaries listed in Finding of Fact "13" by virtue of a "chain of ownership" (tr., p. 215). However, petitioner offered little evidence concerning the operations and nature of its subsidiaries, directly or indirectly owned. Mr. Montgomery also testified, in response to a question as to whether he had looked at "charts" (Exhibit 13) prior to the hearing, that: "I looked at all these. They were all prepared based on information we have based on the forms 5471 that are in the Federal tax return or based on information that would have been supplied to the Federal reserve" (tr., p. 219). A close review of Exhibit "11" (described as a "true copy of the field audit report") to the stipulation between the parties dated April 16, 1993 discloses a listing of 108 subsidiaries. Only three of the subsidiaries listed in Finding of Fact "13" are included: BT Bank of Canada, described as a Canadian bank not included in petitioner's New York combined return because it is "Non NY, No Interco. or improper agreement"; BT (Bankers Trust, presumably) Company International, whose activities are described as financial services and which also was not included in petitioner's New York combined return because it is "Non NY No Interco no improper agreement"; and Malta Properties, a real estate bank, not included because it is "Non NY, No Interco No Improper Agreement." It is not clear why the other 10 subsidiaries listed in Finding of Fact "13" are not included in this listing of 108 subsidiaries. Although somewhat speculative, it may be due to the fact that on the chain of ownership they are more distantly related to petitioner. In any event, the lack of explanation exemplifies the minimal information provided by petitioner concerning the 13 subsidiaries listed in Finding of Fact "13".
>
> Petitioner reserved the right to introduce additional documents into the record after the close of the hearing to establish petitioner's chain of ownership over these subsidiaries described as follows:
>
> Attorney Abitbol:[7] "After consultation with my colleagues and some telephone calls, we decided that the

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[6] We modified finding of fact "13" of the Administrative Law Judge's determination by adding the last six sentences to the paragraph following the chart to more fully reflect the record.

[7] R. Gordon Abitbol is an attorney associated with Hutton & Solomon. Although his names does not appear on the power of attorney appointing Messrs. Moore and Solomon as petitioner's attorneys, petitioner's officer, Martin Linzer, who was present at the hearing, expressly approved of Mr. Abitbol's participation at the hearing.

> best thing to do would be to submit a certified copy of the stock, the record of stock ownership from each of the companies listed in . . . the schedule, Petitioner's 13, demonstrating the chain of ownership" (tr., p. 229).[8]

Documents Submitted After the Hearing

Petitioner, by a letter dated November 30, 1993, described the documents it submitted (on that same date) to establish ownership of the subsidiaries listed in Finding of Fact "13" as follows:

> "1. The taxpayer's original books and records with respect to stock ownership of its subsidiaries are, in fact, electronic, and are kept on a database in a computer. The raw data contained in such database and the reports generated thereby are used by the taxpayer in tax reports and filings, submissions to various State and federal regulatory agencies, etc. Rather than presenting the Court with the raw data concerning stock ownership, which cannot be easily or concisely extracted from such database in a meaningful or easily-understood manner, we have taken the liberty of presenting the Court with reports setting forth the applicable information, i.e., the name of the subsidiary; the total shares of such subsidiary outstanding as of certain dates critical to this proceeding; the name of the entity that owns such subsidiary's shares; the amounts and dates such shares were acquired, as well as the
> nature of such acquisition; and a figure representing the total equity ownership. The accuracy of the data is certified by both Jeffrey Bardos, an officer of the taxpayer and the person principally responsible for maintaining the database, who asserts that the data used in the reports accurately reflects that contained in such database; and by Harry Montgomery, who testified on this issue at the October 22, 1993, hearing. Such certifications appear in the front of the binder.
>
> "2. The binder is arranged as follows: the first page is merely a copy of Petitioner's Exhibit '12,' which serves more or less as a Table of Contents. The first page of each tabbed section is a copy of the page of Petitioner's Exhibit '13' that relates to the particular subsidiary. Behind that page is arranged (by year, if applicable) the above-mentioned reports detailing the chain of ownership, starting with the 'bottom-most' subsidiary and proceeding upwards to Bankers Trust Company, the wholly-owned subsidiary of the taxpayer."

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[8] We modified finding of fact "14" of the Administrative Law Judge's determination by adding the third sentence of the first paragraph regarding Mr. Montgomery's response to a question about "charts" to more fully reflect the record.

A close review of the first "tabbed section" concerning BT Holdings (U.K.) Ltd., as an example, discloses the following. The first page shows a chain of ownership of petitioner owning 100% of Bankers Trust Co., which, in turn, owns 100% of Bankers International Corp., which, in turn, owns 100% of BT Holdings (Europe) Limited, which, in turn, owns 100% of BT Holdings (U.K.) Ltd. The next nine pages are so-called "acquisition reports". The first acquisition report pertains to Bankers Trust Holdings (U.K.) Ltd. as of December 31, 1985 and is in the following format:

"Company Name: Bankers Trust Holdings (U.K.) Ltd.
Total Shares Outstanding: 182,999,900 as of Dec. 31, 1985
Owners Name: BT Holdings (Europe) Limited

Date of Acq.	Type	Number of Shares
December 22, 1983	Transfer	44,666,837
December 22, 1983	Capital Increase	138,333,063
Total		182,999,900
	Equity Ownership	100%"

The second acquisition report also pertains to Bankers Trust Holdings (U.K.) Ltd., updated to December 31, 1986 and shows changes in stock ownership during 1986, in addition to restating the earlier 1983 entries, as follows:

"Date of Acq.	Type	Number of Shares
December 22, 1983	Transfer	44,666,837
December 22, 1983	Capital increase	138,333,063
August 31, 1986	Share reduction	(164,699,900)
October 14, 1986	Stock dividend/new issue	10,000,000
December 29, 1986	Stock dividend/new issue	51,020,408
Total		79,320,408
	Equity Ownership	100%"

The third acquisition report also pertains to Bankers Trust Holdings (U.K.) Ltd., updated to December 31, 1987. This report shows no changes in stock ownership during 1987 and recaps

the entries shown on the 1986 report. The next three acquisition reports pertain to BT Holdings (Europe) Limited as of December 31, 1985, December 31, 1986 and December 31, 1987, respectively. Each shows the owners as Bankers International Corporation with equity ownership of 100%. The only entry on each of the reports is as follows:

Date of Acquisition	Type	Number of Shares
December 8, 1983	Original cost or capital	1,000

The final three acquisition reports in the first tabbed section concerning BT Holdings (U.K.) Ltd. pertain to Bankers International Corporation. Each show the owner as Bankers Trust Company with equity ownership of 100%. Each report shows the same entries:

Date of Acquisition	Type	Number of Shares
February 28, 1960	Original cost or capital	100,000
January 31, 1963	Capital increase	150,000
Total		250,000

Petitioner also submitted on November 30, 1993 "true copies of the complete federal tax returns of the taxpayer for the years 1985, 1986 and 1987" (emphasis in original). Petitioner's representative described his reason for submitting these returns, which consist of three large cartons containing a couple thousand pages, as follows:

> "Upon reviewing the transcript and conferring with the client, we determined that the copies of such returns submitted into evidence by the Division of Taxation, as part of Exhibit B, were not, in fact, complete copies as filed with the Internal Revenue Service. For the sake of completeness, we are submitting the complete returns. We have consulted with John O. Michaelson, Esq., counsel for respondent, in this matter, who indicated that he has no objection to the complete returns becoming part of the official record" (emphasis added).

However, Mr. Michaelson, by a letter dated December 8, 1993 to the Administrative Law Judge, denied such consent:

> "Recently, I received several large boxes of documents that the petitioner is attempting to submit into evidence. Frankly, I was surprised at the petitioner's attempt to submit additional evidence into the record at this late date. This ploy is an attempt to place the Division at a severe disadvantage and is contrary to the Rules of Practice of the Tax Appeals Tribunal.

"The petitioner is attempting to submit a number of affidavits [certifications], several tax returns [the complete Federal tax returns] and a summary prepared by the petitioner which describes the alleged stock ownership of various corporations. The documents being submitted do not include the one thing that the record was kept open for namely, certified copies of the record of stock ownership.

"The Division is being denied its procedural due process rights because we will not be able to cross examine the affiants on the subject matter of the affidavits. Further, we are unable to object on the record to the offer of this new evidence.

"In your closing summary of October 22, 1993, you stated that the record was being kept open for just one reason; to allow for 'the submission of the certified copies of the record of stock ownership.' Your summary goes on to state '[a]ny briefs or other documents not filed in accordance with this schedule will be returned to the party that filed them.' We request that these additional documents be returned to the petitioner and not be considered in your deliberations."

We modify the first paragraph of finding of fact "17" of the Administrative Law Judge's determination to read as follows:

By a letter dated May 13, 1994, petitioner filed its "supplemental reply brief" in accordance with the Administrative Law Judge's order of April 29, 1994.[9] Petitioner appended the following correspondence to this final brief:[10]

Date of Letter	Writer	Addressee	Subject
April 5, 1994	Attorney Abitbol	Assistant Attorney General Carol Fiske	Attorney Fiske's use of (1) affidavits of

[9] By a motion dated April 14, 1993, petitioner sought to amend its petition to assert additional issues, which resulted in the continuation of the hearing. By an order dated August 19, 1993, the Administrative Law Judge permitted petitioner to amend its petition to raise the issue concerning the deduction of 17% of the interest received from indirect subsidiaries in the computation of entire net income.

By a motion dated February 14, 1994, petitioner had sought to sever the second main issue herein, concerning the exclusion of United States obligations and the interest therein in computation of entire net income and capital, and to stay adjudication of such issue pending the final determination of the action for declaratory judgment before the Supreme Court of the State of New York, County of Nassau, entitled Astoria Federal Savings and Loan Association v. State of New York et al (Index No. 93-006014) on the grounds that such issue was the subject of a motion for summary judgment then pending in the Supreme Court action. Petitioner maintained that the 1991 amendment to Public Authorities Law § 1045-u.3, which made it clear that New York City Municipal Water Finance Authority bonds (and the interest thereon) have always been subject to indirect taxation such as franchise taxes, was unconstitutional. Since the constitutionality of such section, as amended, must be presumed by the Administrative Law Judge, petitioner contended that this administrative proceeding should be stayed as to such issue. With its motion papers, petitioner submitted a copy of the Astoria Federal Savings and Loan Association's brief in support of its motion for summary judgment. (Petitioner's representative was also Astoria's representative.) By an order dated April 29, 1994, the Administrative Law Judge denied petitioner's motion to sever and stay and permitted petitioner to submit a supplemental reply brief.

[10] We modified the first paragraph of finding of fact "17" by adding a footnote to clarify the record.

			Domenick R. Sciortino and of William Collins, marked as exhibits in this matter, (ii) an excerpt of the hearing transcript and (iii) Astoria's own Tax Appeals petition in her motion papers and brief in the Astoria Federal Savings & Loan Association declaratory judgment action allegedly violated the secrecy provisions of Tax Law §§ 202 and 1467.
April 7, 1994	Assistant A.G. Fiske	Attorney Abitbol	Tax Department denies violation of secrecy provisions.
April 18, 1994	Attorney Abitbol	Karl Felsen, Records Access Officer for Dept. of Taxation and Finance	Requests copy of full transcript of hearing held in this matter on April 16, 1993 and encloses check in payment.
April 28, 1994	Roberta Moseley Nero, Secretary to the Tax Appeals Tribunal	Attorney Solomon	Transcript will not be provided to Attorney Abitbol because he is not an authorized representative of Bankers Trust.
April 29, 1994	Karl Felsen	Attorney Abitbol	Transcript will not be provided because petitioner's representatives, "Messrs. Hutton and Moore stated that Bankers Trust did not want to waive any confidentiality . . . ."

In footnote "1" of its supplemental brief, petitioner gave the following reason for including the above correspondence in its brief:

> "In response to the summary judgment motion filed by the plaintiff, Astoria Federal Savings & Loan Association ('Astoria') in the declaratory judgment action, the Department filed a cross-motion for

> summary judgment. Attached to this cross-motion as evidentiary exhibits were copies of documents introduced as evidence at the administrative hearing of BTNY, along with excerpts from the hearing transcript itself.
>
> * * *
>
> "This unlawful and unauthorized disclosure must not be condoned. BTNY believes that, aside from the violation of the secrecy provisions of the Tax Law, it is patently improper for one party to a pending administrative proceeding to publicly disclose the testimony and evidence submitted therein without the knowledge and permission of this tribunal and the taxpayer involved. This tribunal took steps on more than one occasion during the hearing to ensure BTNY's privacy, which has now been destroyed by the unilateral acts of the Department and the Attorney General."

By a letter received May 31, 1994, Mr. Michaelson requested that the above-described correspondence be returned to petitioner's representative and that the brief which petitioner filed in the declaratory judgment action of Astoria Federal Savings & Loan Association, which was submitted with its motion papers, not be considered.

The parties executed a stipulation dated April 16, 1993 (Division's Ex. "B"), relevant portions of which have been incorporated herein.

OPINION

NEW YORK CITY MUNICIPAL WATER FINANCE AUTHORITY BONDS

Petitioner alleged in its petition that Article 32 of the Tax Law imposes a tax that impermissibly discriminates against obligations of the United States Government and the interest on such obligations in violation of 31 U.S.C. § 3124. Such discrimination occurs, argues petitioner, because of the allegedly favorable treatment given to bonds of the New York City Municipal Water Finance Authority ("Water Authority") compared to the treatment of Federal obligations. Petitioner alleged that although bonds of the Water Authority and interest earned thereon are excluded from the calculation of franchise taxes, Federal obligations and the interest earned thereon are included. Petitioner maintained that the 1991 amendment to Public Authorities Law § 1045-u.3, which clarified that Water Authority bonds and the interest thereon have always been subject to indirect taxation such as franchise taxes, was unconstitutional. As

a result, petitioner argued that Federal obligations and the interest thereon should be excluded from the measure of petitioner's franchise tax.

The Administrative Law Judge concluded that the Division of Tax Appeals lacked jurisdiction to review the facial constitutionality of a statute. Further, he concluded that, based on the language of Public Authorities Law § 1045-u.3 and the legislative intent relative to its 1991 amendment, Water Authority bonds and interest were not excluded from the calculation of the franchise taxes of bondholders. As a result, obligations of the United States were not treated in a discriminatory fashion. Therefore, petitioner properly included interest from Federal obligations in the measurement of its entire net income for each of the years at issue and, for the years 1985 through 1987, it properly included the value of Federal obligations in the measurement of its taxable assets.

On exception, both petitioner and the Division acknowledge that the Division of Tax Appeals is without jurisdiction to address petitioner's constitutional claim. Although petitioner takes exception to the Administrative Law Judge's conclusion that the value of and interest from its Federal obligations were properly included in the measure of its franchise tax, it provides no argument as to why such conclusion was erroneous. Petitioner simply states:

> "[w]hile acknowledging the jurisdictional limitation of the Division of Tax Appeals, BTNY [petitioner] does not concede any of the substantive arguments concerning legislative intent of the Public Authorities Law. That issue will be decided in a court of appropriate jurisdiction using appropriate evidence . . ." (Petitioner's reply brief, p. 2).

As a result, we see no reason to disturb the determination of the Administrative Law Judge on this issue and affirm it for the reasons set forth in his determination.

EXCLUSION OF EXPENSES ATTRIBUTABLE TO PRODUCTION OF FEDERAL INTEREST

At the hearing, the Division contended that if the income from Federal obligations is excluded from entire net income for purposes of calculating New York franchise taxes, then the deductions for expenses directly and indirectly attributable to the production of such exempt income should be similarly excluded. The Administrative Law Judge concluded that this issue

may not be addressed "since it becomes ripe for determination only if Public Authorities Law § 1045-u.3 is declared unconstitutional on its face" (Determination, conclusion of law "E").

We disagree with the Administrative Law Judge's conclusion. In the event that petitioner successfully established before a court of competent jurisdiction that Article 32 of the Tax Law impermissibly discriminates against Federal obligations and that the interest thereon should be excluded from the measure of petitioner's franchise tax, a refund could not be granted before this issue was resolved.

We note that the Division first raised this contention at the hearing. It does not appear in the petition or amended petition nor in the Division's answer, amended answer or in any of the refund denial letters which the Division issued to petitioner. The Division's auditor testified that his worksheets showing the calculations used to arrive at this "determination" were prepared for the hearing and, in fact, are dated only one day prior to the hearing. However, since petitioner did not object to the presentation of evidence on this issue by the Division, and both parties have submitted briefs on this issue, we will consider it herein.

Petitioner argues that there is no legal basis to support the Division's argument that expenses of interest and deductions indirectly attributable to interest income from Federal obligations should also be excluded in the measurement of its entire net income and the value of its taxable assets. Specifically, petitioner, citing to Tax Law § 1453, asserts that the "starting point in computing entire net income is federal taxable income . . . . The law provides for certain, specific modifications to this total. However, none require the add back of expenses attributable to income subject to federal tax but exempt from State tax. Absent a specific provision requiring such add back, no modification is permitted by law" (Petitioner's brief in support, p. 21). Petitioner asserts that the Division's reliance on section 1462(g) for such authority is wrong.

The Division, on the other hand, argues that Tax Law § 1462(g) allows it the discretion to adjust items of income or deduction to accurately reflect petitioner's income. It argues that the

auditor's calculations are warranted in the event that petitioner succeeds in its constitutional argument as set forth above.

We disagree with the Division. First, although petitioner generally bears the burden of proof on matters before the Division of Tax Appeals, the Division must show that there is a rational basis to support its position. We conclude that no rational basis has been demonstrated in support of the Division's position.

Tax Law § 1462(g), relied on by the Division, provides the following:

> "In case it shall appear to the tax commission that any agreement, understanding or arrangement exists between the taxpayer and any other corporation or any person or firm, whereby the activity, business, income or assets of the taxpayer within the state is improperly or inaccurately reflected, the tax commission is authorized and empowered, in its discretion and in such manner as it may determine, to adjust items of income or deductions in computing entire net income or alternative entire net income . . . ."

There is no allegation made by the Division and no evidence in the record to demonstrate that any such agreement or understanding exists. The existence thereof is a necessary prerequisite to a discretionary adjustment of income or deductions by the Division pursuant to this section. As a result, the Division's argument on this basis must fail.

Second, Tax Law § 1453(e) provides that:

> "There shall be allowed as a deduction in determining entire net income, to the extent not deductible in determining federal taxable income:
>
> * * *
>
> "(2) ordinary and necessary expenses paid or incurred during the taxable year attributable to income which is subject to tax under this article but exempt from federal income tax" (emphasis added).

The Division's witness testified that as the basis for his calculation of expenses indirectly attributable to interest from Federal obligations, he relied on the amount of interest deduction reported by petitioner on its U.S. Corporation Income Tax Return (Form 1120). Since the expenses at issue were deducted from petitioner's Federal taxable income, section 1453(e)(2) does not make their deductibility depend on whether interest from Federal obligations is subject to tax pursuant to Article 32. There is no other provision in Article 32 that supports the

Division's argument. In fact, the Division's witness testified that he was not aware of any policy of the Division or any provision of law that supported this argument.

Third, Tax Law § 1453(e)(12) provides a deduction in determining entire net income for:

> "twenty-two and one-half percent of interest income on obligations of New York state, or of any political subdivision thereof, or of the United States, other than obligations held for resale in connection with regular trading activities."

In Matter of Amsterdam Savings Bank (Tax Appeals Tribunal, March 11, 1993), we rejected the "addback" interpretation of section 1453(e) offered by the Division in this case on the grounds that nothing in the legislative history of the section supported the Division's position. We see no reason to alter our conclusion. We would also point out that the interpretation offered by the Division is inconsistent with TSB-M-87(11)C in which the Division enunciated its policy on the addback of expenses as follows:

> "There are no provisions under Article 32 of the Tax Law to add back any expenses which are attributable to any interest income, dividend income, gains or losses from subsidiary capital or any expenses paid or incurred to purchase or carry obligations of New York State, or of any of its political subdivisions, or of the United States. In addition, Article 32 does not provide for any reduction in the amount on which the . . . 22 1/2% is computed."

In short, if petitioner should be successful in its constitutional argument concerning the exclusion of interest income from certain New York State and Federal obligations from its calculation of tax pursuant to Article 32 of the Tax Law, petitioner will not be required to add back expenses attributable to the production of such interest income as urged herein by the Division.

ALLEGED VIOLATION OF SECRECY PROVISIONS

As the Administrative Law Judge found, petitioner first raised this issue in its post-hearing supplemental reply brief by including therewith copies of correspondence between a member of the law firm of petitioner's representatives and an Assistant Attorney General for the State of New York. This correspondence alleged the disclosure by the Division of certain affidavits marked as exhibits and excerpts from the transcript of the hearing in the instant matter

to an Assistant Attorney General and the use of such material in an action brought in another court in violation of the secrecy provisions of Tax Law § 1467.

Tax Law § 1467 provides, in part, as follows:

> "(a) Except in accordance with the proper judicial order or as otherwise provided by law, it shall be unlawful for the commissioner of taxation and finance, any officer or employee of the department of taxation and finance . . . to divulge or make known in any manner the amount of income or any particulars set forth or disclosed in any return required under this article . . . .
>
> "(b)(1) Any officer or employee of the state who willfully violates the provisions of subsection (a) of this section shall be dismissed from office and be incapable of holding any public office in this state for a period of five years thereafter."

The Administrative Law Judge concluded that:

> "[f]irst, it is observed that petitioner raised this serious issue in a fashion that did not provide the Division with a formal means to respond, which would have been provided to the Division if petitioner had proceeded by motion. Moreover, the more appropriate forum for resolving this matter would seem to be the court in which the documents were allegedly used in violation of the secrecy provisions. In any event, the Division of Tax Appeals would not have the jurisdiction to provide a remedy if, in fact, these provisions had been violated. The penalty specified in Tax Law § 1467(b) is not enforceable by the Division of Tax Appeals, whose powers are specified by statute and do not extend to the imposition of penalties for the violation of secrecy provisions by employees of the Division (see, Tax Law § 2006)" (Determination, conclusion of law "B").

On exception, petitioner does not disagree that the Division of Tax Appeals is without jurisdictional authority to provide a remedy if, in fact, a violation of the secrecy provisions of the Tax Law occurred. Petitioner argues that it does not believe that:

> "merely because an administrative body does not have the jurisdiction to administer a particular remedy it should not make factual and/or legal findings about matters that are clearly within the scope of its experience . . . .
>
> "Petitioner respectfully requests that this Tribunal make a finding of fact that the Division improperly disclosed the material at issue, and a conclusion of law that the secrecy provisions of the Tax Law were violated thereby. Petitioner also requests that this Tribunal issue guidelines with respect to this issue for the future protection of taxpayers" (Petitioner's brief in support, p. 28).

Petitioner annexed to its brief on exception copies of the same correspondence it included with its post-hearing supplemental reply brief.

In opposition, the Division argues that a violation of the secrecy provisions of the Tax Law is a criminal misdemeanor pursuant to Tax Law § 1825. Since the Tax Appeals Tribunal is not a court of general jurisdiction, it cannot review matters concerning alleged criminal activities. However, it argues that even if the Tribunal had jurisdiction, there was no violation of secrecy which occurred. The disclosure made was to the Attorney General in conjunction with ongoing litigation and the information so disclosed contained no identifying details of particular taxpayers.

Although the Administrative Law Judge did not make a specific finding as to the admissibility of the documents appended to petitioner's post-hearing brief, they cannot be considered as part of the record in this case because they were submitted after the hearing record was closed (see, Matter of A & J Auto Repair Corp., Tax Appeals Tribunal, May 6, 1993; Matter of Schoonover, Tax Appeals Tribunal, August 15, 1991). This applies as well to the copies of the same correspondence annexed to petitioner's brief on exception. We agree with the conclusion of the Administrative Law Judge that the Division of Tax Appeals (and, by extension, this Tribunal) is not empowered to consider whether a violation of the provisions of Tax Law § 1467 has occurred or to provide a remedy if a violation did occur. Our jurisdiction is strictly limited by statute (Article 40 of the Tax Law). Therefore, we sustain the determination of the Administrative Law Judge on this issue.

FEDERAL TAX RETURNS

In his determination, the Administrative Law Judge did not accept the complete tax returns of petitioner into evidence since they were submitted subsequent to the hearing.

On exception, petitioner argues that, contrary to the conclusion of the Administrative Law Judge, the Division's representative consented to the submission of the complete tax returns as part of the record prior to transmittal of these documents. Petitioner annexed to its brief on exception copies of correspondence between the Division, petitioner's representative and the

Administrative Law Judge. (These documents were not admitted into evidence by the Administrative Law Judge.)

In opposition, the Division argues that once the hearing record is closed, additional evidence may not be submitted.

It is clear that the hearing record was left open by the Administrative Law Judge to receive evidence of stock ownership of subsidiaries from petitioner. The documents submitted on this issue were accepted into evidence by the Administrative Law Judge. The Administrative Law Judge held that unless the Division's representative consented to the submission of such returns after the hearing was concluded or petitioner had obtained permission of the Administrative Law Judge to submit them before the close of the hearing, they should be excluded from the hearing record. Finding that no such consent or permission was present, the Administrative Law Judge refused to make these returns part of the record. We agree.

DEDUCTION OF 17% OF INTEREST INCOME FROM INDIRECT SUBSIDIARIES

The Administrative Law Judge reviewed the provisions of Tax Law §§ 1450 and 1453(e)(11)(I), 20 NYCRR 16-2.22 (as in effect for the relevant period here at issue) and the decision of this Tribunal in Matter of Racal Corp. & Decca Electronics (Tax Appeals Tribunal, May 13, 1993) and concluded that:

> "[c]onsequently, in the matter at hand it must be determined whether petitioner controlled all aspects of the operation and management of the indirect subsidiaries listed in Finding of Fact '13'. Petitioner has failed to prove that it did so. In this regard, petitioner's proof is minimal as noted in Finding of Fact '14'. The situation at hand is quite different from that in Matter of The Racal Corporation and Decca Electronics (supra) where the Division stipulated that the taxpayer therein had the following control over the indirect subsidiaries at issue:
>
> > "(i) Absolute control over the election and removal of officers and directors;
> >
> > "(ii) Absolute control over all operational, tax and financial matters;
> >
> > "(iii) Absolute power to cause dividends to be declared and paid;

> "(iv) Absolute right to sell or pledge all stock of the subsidiaries; and
>
> "(v) Absolute power to maintain a shareholder derivative action" (Determination, conclusion of law "J").

On exception, petitioner argues that, based on the evidence and testimony presented, petitioner has demonstrated that it had "actual beneficial ownership" of the subsidiaries at issue. It argues that the Administrative Law Judge improperly substituted a standard of "absolute control" for "actual beneficial ownership." Petitioner's witness testified that the same indicia of beneficial ownership required by the Division in Xerox Corp. v. Dept. of Taxation & Fin. (Sup Ct, Monroe County, January 12, 1987, Provenzano, J. [TSB-H-87(25)C], revd 140 AD2d 945, 529 NYS2d 623, lv denied 72 NY2d 809, 534 NYS2d 666) were present in the relationship of petitioner to its indirect subsidiaries. In fact, argues petitioner:

> "any time a corporation has 'actual beneficial ownership' of 100% of the stock of a subsidiary, it has the power to 'control all aspects' of its management and operations, since through its chain of ownership, it has the power to control stockholder voting, control membership on the board of directors and the personnel employed by such subsidiaries. There is no greater degree of control than that exemplified by 100% stock ownership" (Petitioner's brief in support, pp. 18-19).

In opposition, the Division argues that "[t]he petitioner must prove both stock ownership and control of all aspects of the foreign entities in order to meet the standard described in Racal" (Division's brief, pp. 18-19). The Division argues that petitioner has neither presented any credible evidence regarding stock ownership nor shown that petitioner controlled any aspect of the operations and management of its alleged subsidiaries.

We affirm the determination of the Administrative Law Judge on this issue for the reasons set forth below.

For the period at issue herein, Tax Law § 1453(e)(11)(I) allowed a deduction for 17% of interest income from subsidiary capital in determining the entire net income of a banking corporation. "Subsidiary" and "subsidiary capital" are defined in Tax Law § 1450 as follows:

> "(d) The term 'subsidiary' means a corporation or association of which over fifty percent of the number of shares of stock entitling the

> holders thereof to vote for the election of directors or trustees is owned by the taxpayer.
>
> "(e) The term 'subsidiary capital' means investments in the stock of subsidiaries and any indebtedness from subsidiaries . . . ."

In his determination, the Administrative Law Judge quotes the broad definition of "subsidiary," as found in the Division's regulations concerning franchise tax on banking corporations at 20 NYCRR former 3-6.2, in relevant part, as follows:

> "(a) The term subsidiary means a corporation which is controlled by the taxpayer, by reason of the taxpayer's ownership of more than 50 percent of the total number of the shares of stock of such corporation, issued and outstanding, which entitle the holder of the shares to vote at elections of its directors or trustees . . . .
>
> "(b) The test of ownership is actual beneficial ownership, rather than mere record title as shown by the stock books of the issuing corporation. A corporation will not be considered to be a subsidiary because more than 50 percent of the shares of its voting stock is registered in the taxpayer's name, unless the taxpayer is the actual beneficial owner of such stock. However, a corporation will not be considered a subsidiary if more than 50 percent of the shares of its voting stock is not registered in the taxpayer's name, unless the taxpayer submits proof that it is the actual beneficial owner of such stock" (Determination, conclusion of law "I").

Although that section was amended (effective January 19, 1994) to provide that "[a]ctual beneficial ownership of stock does not mean indirect ownership or control of a corporation through a corporate structure consisting of several tiers and/or chains" (20 NYCRR 16-2.22[b]), neither party excepted to the conclusion of the Administrative Law Judge that the amended regulation was not to be applied retroactively to the years at issue herein.

As we stated in Matter of Racal Corp. & Decca Electronics (supra):

> "the question we are presented with is not one of simply interpreting and applying the statutory definition of subsidiary, but instead, of applying the regulation promulgated by the Division that defines a subsidiary in terms of control and defines ownership in terms of beneficial ownership."

In Racal, we relied on Yelencsics v. Commissioner (74 TC 1513, at 1527) which defined "beneficial ownership" as "marked by command over property or enjoyment of its economic benefits." We noted that, in TSB-M-79(1)C, the Division defined "beneficial ownership" to

mean: "[t]he stockholder has beneficial ownership when it owns indirectly and controls the voting stock of another corporation." In Xerox Corp. v. Dept. of Taxation & Fin. (supra), the Division argued that whether a second-tier subsidiary was a subsidiary was a question of fact. In that case, the Division presented an affidavit pointing out that beneficial ownership is indicated by the absolute right to sell or pledge the stock, receive dividends from the stock and vote and maintain a shareholder derivative action. While the measure of control exercised by petitioner is relevant in determining whether petitioner had "actual beneficial ownership" of the corporations at issue herein, we agree with petitioner that the Administrative Law Judge's conclusion that "it must be determined whether petitioner controlled all aspects of the operation and management of the indirect subsidiaries" (Determination, conclusion of law "J") is too strict a construction of the applicable provisions of the Tax Law and their interpreting regulation.

However, we do not agree with petitioner that it has demonstrated that it is the actual beneficial owner of the corporations for which it has claimed a deduction pursuant to Tax Law § 1453(e)(11)(I). In Racal, the parties had stipulated to the petitioner's absolute control of all aspects of the second-tier subsidiary's operation. No such stipulation was made in the present case. Here, since more than 50% of the shares of the voting stock of those corporations claimed as subsidiaries is not registered in petitioner's name, petitioner had the burden to submit proof that it is the actual beneficial owner of such stock (20 NYCRR 16-2.22[b]). To do so, petitioner must show that it: had "command over property or enjoyment of its economic benefits"; "owns indirectly and controls the voting stock of another corporation"; or had the "absolute right to sell or pledge the stock, receive dividends from the stock and vote and maintain a shareholder derivative action" (Matter of Racal Corp. & Decca Electronics, supra). This petitioner did not do.

As set forth in amended findings of fact "13" and "14," petitioner's witness testified that the amounts it claimed to have received as subsidiary interest came from petitioner's books and records. However, no books and records were brought to the hearing. While petitioner's witness had "no question in his mind" that Bankers Trust Company (petitioner's principal

subsidiary) owned and controlled the subsidiaries at issue by virtue of a chain of ownership, petitioner offered little evidence concerning the operations and nature of its subsidiaries. Without offering any first-hand knowledge of the degree of control exercised by petitioner, the witness testified that the chain of ownership charts were prepared from information on the Federal tax return or information that would have been supplied to the Federal Reserve.

Petitioner's arguments are summed up in its brief in support of its exception as follows:

> "any time a corporation has 'actual beneficial ownership' of 100% of the stock of a subsidiary, it has the power to 'control all aspects' of its management and operations, since through its chain of ownership, it has the power to control stockholder voting, control membership on the board of directors and the personnel employed by such subsidiaries. There is no greater degree of control than that exemplified by 100% stock ownership" (Petitioner's brief, pp. 18-19).

However, neither Tax Law § 1450 nor the regulation interpreting it provide that indirect ownership of 100% of the stock of a second-tier subsidiary corporation conclusively demonstrates actual control of such corporation or actual beneficial ownership of its stock. If the only issue is ownership of 100% of the stock of a corporation claimed to be a subsidiary, then the holding in Racal is superfluous. In Racal, the taxpayer was the indirect owner of 100% of the shares of each of the corporations claimed by it to be subsidiaries. However, it was the indicia of control over those corporations and of their beneficial ownership that formed the basis of the Tribunal's decision and not the 100% indirect ownership of their stock. As a result, we affirm the determination of the Administrative Law Judge sustaining the Division's denial of refund on this issue.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Bankers Trust New York Corporation is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petition of Bankers Trust New York Corporation is denied; and

4. The refund claim denials dated October 31, 1990, March 8, 1991 and January 29, 1992 are sustained.

DATED: Troy, New York
March 14, 1996

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

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

/s/Donald C. DeWitt
Donald C. DeWitt
Commissioner