

BUREAU OF LAW

MEMORANDUM

*Corporation Tax Determinations
A-Z
Diamond International
Corporation*

TO: Commissioners Murphy, Macduff and Conlon
FROM: E. H. Best, Counsel
SUBJECT: **DIAMOND INTERNATIONAL CORPORATION**
For revision or refund of franchise taxes under Article 9-A of the Tax Law for the calendar years 1957 to 1963, inclusive

The issue involved herein is whether certain short-term notes should be included in investment capital as contended by the Corporation Tax Bureau and the income therefrom included in investment income or to be deemed a part of the taxpayer's business capital and the income therefrom allocable business income as contended by the taxpayer.

During the years in question, the taxpayer purchased short-term notes directly from the following makers:

Associated Investment Company
CIT Financial Corporation
Commercial Credit Company
General Motors Acceptance Corporation
General Electric Corporation
Sears-Roebuck Acceptance Corporation
Pacific Finance Corporation

These notes were purchased by the taxpayer for the purpose of investing its available cash.

The interest income from such notes and claimed tax over-assessments as a result of their inclusion in investment income is as follows:

Year	Income	Tax
1957	\$ 56,168	\$ 4,118.19
1958	89,894	1,537.93
1959	156,403	886.04
1960	323,139	1,779.36
1961	355,609	492.20
1962	270,263	35,524.99
1963	51,164	226.05

The taxpayer argued that it does not buy these short-term notes for investment purposes but merely puts available cash into

short-term notes in order to earn interest for the short period of time the cash would otherwise be sitting idle in a bank, until quarterly tax payments and dividends are paid.

The hearing officer is of the opinion that the notes constitute investment capital and the income therefrom constituted investment income as defined by Section 208, subdivisions 5 and 6 of the Tax Law and 20 NYCRR 3.32(e). The regulation cited provides that investment capital does not include, "corporate obligations not commonly known as securities, such as real property or chattel mortgages, contracts of sale, purchase money obligations, short-term notes, bills of lading, bills of exchange and other commercial instruments", which are payable by their terms on demand or within one year from the date incurred.

While a first reading of the regulation would seem to exclude short-term notes from investment capital, on June 6, 1962, I issued an opinion (herein attached) that the proper construction of the regulation is that the "short-term notes" excluded from investment capital are only those resulting from the business activities of the taxpayer, particularly those received in payment for goods or services rendered. The matter, however, is not entirely free from doubt. See attached to the files a previous memorandum dated March 15, 1960 and letter dated March 17, 1960 concerning contrary treatment of short-term notes.

Since, however, the short-term notes herein were not received in payment for goods sold or services rendered but were investments of capital, I am in agreement with the hearing officer that the interest from the short-term notes was investment income and not business income.

Please sign three copies of the determination and return the entire file together with such signed copies to the Law Bureau for further disposition.

/s/

E. H. BEST

Counsel

FVD:rlp
Enc.
October 16, 1967

10-18-67

STATE OF NEW YORK

THE STATE TAX COMMISSION

In the Matter of the Applications ;
of ;
DIAMOND INTERNATIONAL CORPORATION ;
for revision or refund of franchise ;
taxes under Article 9-A of the Tax ;
Law for the calendar years 1957 to ;
1963, inclusive. ;

Diamond International Corporation, the taxpayer herein, having filed applications for revision or refund of franchise taxes for the calendar years 1957 to 1963, inclusive, and a hearing having been held in connection therewith at the office of the State Tax Commission in New York City on February 3, 1967 before Donald E. Gilhooly, Hearing Officer of the Department of Taxation and Finance, at which hearing Vernon Grout, Comptroller, and Leo H. Wiest, Tax Manager, of the taxpayer, appeared personally and testified, and the record having been duly examined and considered by the Tax Commission,

It is hereby found:

(1) That the taxpayer incorporated in Delaware December 26, 1930, and changed its name October 23, 1964 from Diamond National Corporation to Diamond International Corporation, and has been authorized in New York State since March 31, 1936;

(2) That on the basis of the reports filed and an examination made by the tax commission's field auditors, taxes were reaudited and restated on February 25, 1966 for the years 1957 through 1959, audited and stated on February 25, 1966 for the year 1960, recomputed on February 25, 1966 for the years 1961 and 1962 and on November 15, 1966 for the year 1963, as follows:

	<u>1957</u>	<u>1958</u>	<u>1959</u>
Business Income	\$10,164,554.00	\$9,567,726.00	\$14,788,028.00
Business allocation percentage	11.3251	09.2998	09.1239
Allocated Business Income	1,151,146.00	889,779.00	1,349,245.00
Investment Income	897,855.00	370,978.00	325,786.00
Investment Allocation percentage	07.9313	06.6510	03.7923
Allocated Investment Income	71,212.00	24,674.00	12,355.00
Total Allocated Income	1,222,358.00	914,453.00	1,361,600.00
Tax at 5½%	67,229.69	50,249.92	74,888.00
Plus Subsidiary Capital Tax	568.49	646.49	994.17
Penalty	189.15	- 0 -	- 0 -
Total Tax & Penalty \$	\$ 67,987.33	\$ 50,941.41	\$ 75,882.17

	<u>1960</u>	<u>1961</u>	<u>1962</u>
Business Income	\$19,621,853.00	19,969,132.00	17,421,183.00
Business allocation percentage	10.8219	10.5892	11.0185
Allocated Business Income	2,123,457.00	2,114,571.00	1,919,553.00
Investment Income	677,156.00	553,687.00	15,070,322.00
Investment Allocation percentage	06.3868	06.6861	04.4361
Allocated Investment Income	43,272.00	37,020.00	668,535.00
Total Allocated Income	2,166,729.00	2,151,591.00	2,588,088.00
Tax at 5½%	119,170.10	118,337.91	142,344.84
Plus Subsidiary Capital Tax	1,329.62	529.71	492.74
Penalty	1,593.57	- 0 -	- 0 -
Total Tax & Penalty \$	\$ 122,093.29	\$ 118,867.22	\$ 142,837.58

	<u>1963</u>
Business Income	\$23,567,036.00
Business Allocation percentage	10.1364
Allocated Business Income	2,388,849.00
Investment Income	211,254.00
Investment Allocation percentage	08.0324
Allocated Investment Income	16,969.00
Total Allocated Income	2,405,818.00
Tax at 5½%	132,319.98
Plus Subsidiary Capital Tax	- 0 -
Penalty	- 0 -
Total Tax	\$ 132,319.98

(3) That based on the field audit examination, short-term notes having a maturity of less than one year, which were purchased by the taxpayer directly from the following financial corporations as a means of investing its available cash, were classified as investment capital and included in the calculation

of the investment allocation percentage, and the interest therefrom was included in investment income:

C.I.T. Financial Corporation
Associates Investment Company
General Motors Acceptance Corporation
Commercial Credit Company
General Electric Credit Corporation
Sears Roebuck Acceptance Corp.
Pacific Finance Corporation

(4) That applications for revision or refund were filed on April 14, 1966 for the years 1957 through 1962 and on June 15, 1966 for the year 1963;

(5) That Section 208.5 of the Tax Law reads, in part, as follows:

"The term 'investment capital' means investments in stocks, bonds and other securities, corporate and governmental, not held for sale to customers in the regular course of business * * * ;"

(6) That Section 208.6 of the Tax Law reads, in part, as follows:

"The term 'investment income' means income, including capital gains in excess of capital losses, from investment capital, * * * * ;"

(7) That Section 208.7 of the Tax Law reads, in part, as follows:

"The term 'business capital' means all assets, other than subsidiary capital, investment capital, and * * * * * ;"

(8) That Section 3.31 c of Ruling of the State Tax Commission issued March 14, 1962 reads as follows:

"The 'other securities' referred to in the definition of investment capital are limited to securities issued by governmental bodies and securities issued by corporations, of a like nature as stocks and bonds, which are customarily sold in the open market or on a recognized exchange, designed as a means of investment, and issued for the purpose of financing corporate enterprises and providing a distribution of rights in, or obligations of, such enterprises. Such 'other securities' thus include debentures, notes and certificates of indebtedness which have many of the essential characteristics of bonds, and certificates of interest and other instruments evidencing proprietorship rights in corporate enterprises which have many of the essential characteristics of stock. They do not include corporate obligations not commonly

known as securities, such as real property or chattel mortgages, contracts of sale, purchase money obligations, short-term notes, bills of lading, bills of exchange and other commercial instruments."

Upon the foregoing findings and upon all the evidence presented, it is hereby

DETERMINED:

(A) That the short-term notes constitute "other securities" as contemplated by Section 208.5 of the Tax Law and Section 3.31 c of Ruling of State Tax Commission, and were properly classified as investment capital as such notes are issued for the purpose of financing the activities of the issuers, are designed as a means of investment, did not result from the business activities of the taxpayer, and therefore did not constitute business capital;

(B) That the income from the short-term notes was properly classified as investment income and allocated by the investment allocation percentage;

(C) That the taxes and penalties as shown at Item (2) above are affirmed as assessed;

(D) That the aforesaid taxes do not include taxes or other charges which are not legally due.

Dated: Albany, New York

this 27th day of November 1967

THE STATE TAX COMMISSION

/s/

JOSEPH H. MURPHY
COMMISSIONER

COMMISSIONER

/s/

WALTER MACLYN CONLON
COMMISSIONER