

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of Petition

of

NORTON COMPANY

for redetermination of deficiency
of franchise tax under Article 9-A
of the tax law for 1967, 1968 and
1969.

Norton Company having filed a petition for redetermination of deficiencies under Article 9-A of the tax law for 1967, 1968 and 1969 and a hearing having been held on October 26, 1972 before John J. Genevich, Hearing Officer of the Department of Taxation and Finance, at the office of the State Tax Commission, State Campus, Albany, New York, at which hearing S. B. Lee, Jr., Director of Taxes of Norton Company, appeared personally and testified, and the record having been duly examined and considered by the State Tax Commission,

It is hereby found:

(1) Norton Company manufactures and sells abrasive products and files a combined return with its wholly owned subsidiary, Norton International Inc., which handles all export sales of the parent. The parent also owns the stock of and has made advances to numerous other subsidiaries, which are not included in the combined report.

(2) Based on a field audit examination, the Corporation Tax Bureau issued notices of deficiency in the amounts of \$9,274.12 for 1967, \$12,041.81 for 1968 and \$11,227.41 for 1969. The taxpayer filed timely petition for redetermination of deficiencies. The only amounts in dispute are disallowances of interest expense attributable to subsidiary capital, computed by the Corporation Tax Bureau as follows:

	<u>1967</u>	<u>1968</u>	<u>1969</u>
Subsidiary assets	\$ 81,722,986.00	\$ 80,442,792.00	\$ 70,691,245.00
Total assets	240,950,057.00	244,358,690.00	252,497,257.00
Subsidiary %	33.92	32.92	28.00
Interest expense deducted	1,916,549.60	2,127,877.56	2,286,878.12
Interest expense disallowed	650,093.62	700,497.29	640,325.87
Business allocation %	23.05769	21.210861	19.429918
Allocated interest expense	149,896.57	148,581.51	124,414.79
Deficiency at 5-1/2%	8,244.31		
Deficiency at 7%		10,400.71	8,709.04

(3) Included in interest expense deducted on the returns was interest paid on Federal and State income taxes in the amounts of \$7,711.60 for 1967, \$34,667.56 for 1968 and \$15,024.12 for 1969. Subtraction of such interest expense from total interest expense deducted on the returns results in revised deficiencies, due to addback of interest attributable to subsidiary capital, as follows:

	<u>1967</u>	<u>1968</u>	<u>1969</u>
Interest expense deducted	\$1,916,549.60	\$2,127,877.56	\$2,286,878.12
Less above amounts	7,711.60	34,667.56	15,024.12
Adjusted interest expense	1,908,838.00	2,093,210.00	2,271,854.00
Subsidiary %	33.92	32.92	28.00
Interest expense disallowed	647,478.00	689,085.00	636,119.00
Business allocation %	23.05769	21.210861	19.429918
Allocated interest	149,293.00	146,161.00	123,587.00
Revised deficiency at 5-1/2%	8,211.12		
Revised deficiency at 7%		10,231.27	8,651.79

The total revised deficiencies are as follows:

	<u>1967</u>	<u>1968</u>	<u>1969</u>
Agreed portion of deficiency	\$1,029.81	\$ 1,641.10	\$ 2,518.37
Revised portion of deficiency	<u>8,211.12</u>	<u>10,231.27</u>	<u>8,651.79</u>
Total revised deficiency	\$9,240.93	\$11,872.37	\$11,170.16

The foregoing adjustments were based on Section 208.9 (b)(6) of the tax law which states:

"(b) Entire net income shall be determined without the exclusion, deduction or credit of:

"(6) in the discretion of the tax commission, any amount of interest directly or indirectly and any other amount directly attributable as a carrying charge or otherwise to subsidiary capital or to income, gains or losses from subsidiary capital;"

(4) In computing its entire net income for each year, the taxpayer eliminated the following income from subsidiary capital:

	<u>1967</u>	<u>1968</u>	<u>1969</u>
Dividends from subsidiary capital	\$4,270,721.28	\$5,042,338.12	\$6,246,619.07
Interest from subsidiary capital	<u>861,175.20</u>	<u>507,393.99</u>	<u>405,652.43</u>
Total income eliminated	\$5,131,896.48	\$5,549,732.11	\$6,652,271.50

The above income was eliminated pursuant to Section 208.9 (a)(1) of the tax law, which reads in part:

"(a) Entire net income shall not include:
"(1) income, gains and losses from subsidiary capital***."

The State Tax Commission hereby

DECIDES:

(A) Since a portion of the taxpayer's borrowings is used to make investments in and advances to subsidiaries, a portion of taxpayer's interest expense is attributable to subsidiary capital.

(B) It has been the consistent policy of the Commission to disallow interest expense attributable to subsidiary capital in accordance with Section 208.9 (b)(6) of the tax law. Such disallowance is required to prevent the taxpayer from receiving a double benefit since Section 208.9 (a)(1) provides that the taxpayer may exclude income from subsidiary capital. The exclusions by the taxpayer, as indicated in Item (4), are substantially more than the interest expense disallowances computed in Item (3).

(C) The total revised deficiencies set forth in Item (3) are affirmed as correct, together with interest in accordance with Section 1084 of the tax law.

Dated: Albany, New York

this 18th day of May 1973.

STATE TAX COMMISSION

Norman Gallman
President

Bruce Presley
Commissioner

Milton Koerner
Commissioner