

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of
U.S. Summit Corporation :

AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Corporation :
Franchise Tax under Article 9A of the Tax Law :
for the Years Ended Dec. 31, 1977 - Dec. 31, 1979.

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 23rd day of May, 1985, he served the within notice of decision by certified mail upon U.S. Summit Corporation, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

U.S. Summit Corporation
600 Third Avenue
New York, NY 10017

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
23rd day of May, 1985.

David Parchuck

Annice R. Haglund
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
U.S. Summit Corporation :

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for Redetermination of a Deficiency or Revision :
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Franchise Tax under Article 9A of the Tax Law :
for the Years Ended Dec. 31, 1977 - Dec. 31, 1979.

State of New York :
ss.:
County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 23rd day of May, 1985, he served the within notice of decision by certified mail upon Ralph A. Pastore, the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Ralph A. Pastore
George R. Funaro & Co.
420 Lexington Avenue. Rm 2820
New York, NY 10170

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this
23rd day of May, 1985.

David Parchuck

Samuel A. Shuchman
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

May 23, 1985

U.S. Summit Corporation
600 Third Avenue
New York, NY 10017

Gentlemen:

Please take notice of the decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1090 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Ralph A. Pastore
George R. Funaro & Co.
420 Lexington Avenue. Rm 2820
New York, NY 10170
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
of	:	
U.S. SUMMIT CORPORATION	:	DECISION
for Redetermination of a Deficiency or for	:	
Refund of Corporation Franchise Tax under	:	
Article 9-A of the Tax Law for the Years Ended	:	
December 31, 1977 through December 31, 1979.	:	

Petitioner, U.S. Summit Corporation, 600 Third Avenue, New York, New York 10017, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the years ended December 31, 1977 through December 31, 1979 (File No. 40023).

A formal hearing was held before Frank W. Barrie, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on October 17, 1984 at 1:15 P.M. Petitioner appeared by George R. Funaro & Co., P.C. (Ralph A. Pastore, C.P.A.). The Audit Division appeared by John P. Dugan, Esq. (Lawrence A. Newman, Esq., of counsel).

ISSUE

Whether the Audit Division properly determined petitioner's tax on subsidiary capital and interest attributable to subsidiary capital.

FINDINGS OF FACT

1. Petitioner, U.S. Summit Corporation, filed New York State corporation franchise tax reports for the years ended December 31, 1977, 1978 and 1979. On each of such reports, petitioner failed to compute the tax on subsidiary capital imposed by section 210.1(b) of the Tax Law. Petitioner also failed to

compute interest attributable to subsidiary capital as required by section 208.9(b)(6) of the Tax Law.

2. On September 3, 1982, as the result of a field audit, the Audit Division issued three notices of deficiency against petitioner as follows:

<u>Period Ended</u>	<u>Tax</u>	<u>Interest</u>	<u>Total Due</u>
December 31, 1977	\$6,919.00	\$3,253.00	\$10,172.00
December 31, 1978	23.00	9.00	32.00
December 31, 1979	2,025.00	608.00	2,633.00

The deficiencies were based in part on petitioner's failure to compute the tax on subsidiary capital and the interest attributable to subsidiary capital.

3. Petitioner is a trading company engaged in the export of pharmaceuticals and nutritional products such as infant formula. One of its subsidiaries, Pure Laboratories, Inc. ("Pure"), was inactive during the years in issue, but had been engaged in manufacturing pharmaceuticals until 1968 at which time petitioner's managers decided to liquidate Pure and sold all of Pure's existing inventory, raw materials and production equipment. The building housing Pure's operations was owned by Pure and leased to unrelated corporations until 1977 when it was sold. At this point, Pure became completely inactive. In 1977 petitioner made advances to Pure. These advances were carried on Pure's books as liabilities and on petitioner's books as receivables throughout the years in issue. Pure also received a small amount of income during the years in issue consisting mainly of cash receipts from back rental payments. Petitioner handled all collections of cash receipts for Pure during the years in issue.

4. On audit, the auditor, in computing subsidiary capital with respect to petitioner, added Pure's stockholders' equity, which was a deficit for the years in issue, to the advances made by petitioner less loans to petitioner from Pure. Since the equity was less than zero, the auditor set the value at

zero prior to adding the advances because the regulations provide that no subsidiary may be valued at less than zero. The auditor computed the subsidiary capital of petitioner in this fashion for each year in issue. The average fair market value of petitioner's subsidiary capital was then determined by adding the beginning and ending amounts of subsidiary capital for each year and dividing by two.

5. To determine the interest attributable to subsidiary capital, the auditor divided the average cost of investment in subsidiary capital by petitioner's total assets. The resulting percentage was applied to petitioner's total interest expense to arrive at interest attributable to subsidiary capital. The average cost of investment in subsidiary capital was obtained by adding the beginning and end of year amounts of capital stock of Pure to the advances to Pure by petitioner and dividing by two.

6. Petitioner maintains that, in computing the amount of subsidiary capital, the advances made by petitioner to Pure in 1977 should have been valued at zero because there was little or no chance that these advances would ever be recovered by petitioner. Petitioner, however, offered no explanation as to why the advances were still carried on its books as receivables and why no attempt had been made to write the advances off as bad debts for either accounting or tax purposes.

CONCLUSIONS OF LAW

A. That section 208.9 of the Tax Law provides, in pertinent part:

"The term 'entire net income' means total net income from all sources...

* * *

(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."

B. That, in addition to the tax measured by entire net income or other alternative basis, section 210.1(b) of the Tax Law imposes a tax measured by subsidiary capital. Section 208.4 of the Tax Law defines "subsidiary capital" as follows:

"The term 'subsidiary capital' means investments in the stock of subsidiaries and any indebtedness from subsidiaries, exclusive of accounts receivable acquired in the ordinary course of trade or business for services rendered or for sales of property held primarily for sale to customers, whether or not evidenced by written instrument, on which interest is not claimed and deducted by the subsidiary for purposes of taxation under articles nine-a, nine-b, nine-c, thirty-two or thirty-three of this chapter, provided, however, that, in the discretion of the tax commission, there shall be deducted from subsidiary capital any liabilities payable by their terms on demand or within one year from the date incurred, other than loans or advances outstanding for more than a year as of any date during the year covered by the report, which are attributable to subsidiary capital;..."

C. That 20 NYCRR 3-6.4 provides for the computation of subsidiary capital as follows:

"The amount of subsidiary capital of the taxpayer (parent) is determined by computing the average fair market value during the period covered by the report of all the assets of the taxpayer which constitute subsidiary capital, less certain liabilities required to be deducted... Average fair market value is determined in the manner which is described in section 3-4.6 of this Part. In no event may a subsidiary be valued at less than 'zero'."

D. That petitioner continued to carry the advances made to Pure as receivables on its books throughout the years in issue and likewise Pure carried the advances as liabilities. Inasmuch as petitioner chose to treat the advances as an asset and made no attempt to claim the advances as bad debts, either for accounting or tax purposes, it cannot now claim that the advances

were worthless. Having chosen to arrange its books to treat the advances as an asset, it must accept the tax consequences thereof. The Audit Division, therefore, properly included the advances at the average value asserted by petitioner in its books and records in the computation of subsidiary capital for purposes of section 208.9(b)(6) and 210.1(b) of the Tax Law.

E. That the petition of U.S. Summit Corporation is denied and the notices of deficiency issued September 3, 1982 are sustained.

DATED: Albany, New York

STATE TAX COMMISSION

MAY 23 1985

*I abstain.
Rodrigo Arce*

PRESIDENT

Francis R. Kolm

COMMISSIONER

Mark J. Judd

COMMISSIONER