L-9 (11-60)

Minutes of Bur. of Law Determinations A-2

BUREAU OF LAW

MEMORANDUM

Port Chester Electrical Constr. Corp. and Carroll-Ratner Corp.

TO: Commissioners Murphy, Macduff & Conlon

FROM: Solomon Sies, Hearing Officer

SUBJECT: PORT CHESTER ELECTRICAL CONST. CORP. and CARROLL-RATNER CORP.---
Joint Venture

(also x-ref'd under Corp. Tax Determinations)

1957 Assessment No. B-785682

PORT CHESTER ELECTRICAL CONST. CORP. and GEORGE H. McKEE, INC.---
Joint Venture

x-ref.

1957 Assessment No. B-784987

Article 16-A

A hearing with reference to the above matters was held before me at 80 Centre Street, New York City, N.Y. on September 18, 1964. The appearances and the evidence produced were as shown in the stenographic minutes and exhibits submitted herewith.

Since identical issues of fact and law are in issue in both cases, a combined hearing was held in the above matters by consent.

The issues involved herein are: (1) the amount of the allowable exemption of a joint venture under Section 386-f of the Tax Law for the distributive share of a partner thereof which is taxable under Article 16-A of the Tax Law where the member partner, a corporation, is entitled to an allocation of its net income by reason of carrying on a business within and without the State under Article 9-A of the Tax Law; and (2) whether two corporations engaged in a joint venture are each entitled to salary credit under Section 386-e of the Tax Law and Article 13 of the Business Tax Regulations.

Port Chester Electrical Construction Corp., Carroll-Ratner Corp. and George H. McKee, Inc. are all domestic corporations organized under the laws of New York State. Port Chester Electrical Construction Corp. entered into two joint ventures, one with George H. McKee, Inc. on April 11, 1956 and one with Carroll-Ratner Corp. on March 25, 1955. The joint venturers elected to report their income for tax purposes on the long-term contract of accounting basis and reported their entire income for the year 1957 when the work was completed. The contracts in question were entered into by the joint venturers for electrical construction to be performed solely within the State of New York. Port Chester Electrical Construction Corp., as one of the joint venturers, in filing its corporation franchise tax return under Article 9-A of the Tax Law allocated its

income to both within and without the State of New York, the allocation percentage being .629389%. Carroll-Ratner Corp. and George H. McKee, Inc. did not claim any allocation of income to both within and without the state on the franchise tax returns filed by them. On the unincorporated business tax returns filed by the joint ventures heretofore mentioned under Article 16-A of the Tax Law, they claimed a full exemption of their entire net income for the year 1957 so that no tax was paid upon the filing of the returns.

Section 386-f of the Tax Law was amended by Chapter 387 of the Laws of 1949. In the 1949 New York State Legislative Manual, Page 300, it is stated:

> "This bill would limit the exemption for the distributive share of a partner allowed in computing the unincorporated business income tax to the amount allocable to New York in the return filed by the partner under Articles 9-A, 9-B, 9-C or 16-A of the Tax Law.
>
> Under the present provisions of said Section 386-f an exemption is allowed in computing the net income of an unincorporated business for the distributive share of a partner therein where such share is included in the partner's return filed under Articles 9-A, 9-B, 9-C or 16-A. This exemption was allowed in order to avoid double taxation of the same income--once in the hands of the unincorporated business, such as a joint venture, and again in the hands of the partner's in the joint venture. The present statute also provides that in computing net income taxable to the partner joint venture income is allocated within and without the State in accordance with an allocation formula based upon the partner's other activities within and without the State.
>
> Experience has shown, however, that the allowance of the exemption for the entire distributive share of a partner in computing the taxable income of a joint venture, results in a considerable portion of the income escaping taxation entirely. Thus, if the net income of a joint venture, amounting to $100,000.00 is allocable wholly to New York, a corporate partner having a 50 per cent interest would in its corporate franchise tax report filed under Article 9-A include its distributive share of $50,000.00 in its entire net income and the joint venture would be allowed an exemption for $50,000.00. However, if the corporate partner's other activities within and without the State in allocating only 10 per cent of its income to New York, only $5,000.00 of its distributive share would be subject to the tax computed on income under Article 9-A. Thus, under the present law, the joint venture obtains the benefit of a $50,000.00

exemption even though only $5,000.00 is actually subject to tax in New York. In such circumstances, the exemption allowed the joint venture should be limited to $5,000.00.

The amendment proposed by this bill would accomplish this by limiting the exemption allowed the joint venture to that portion of a partner's distributive share allocable to New York whether the partner is taxable as a corporation under Article 9-A, 9-B, 9-C or as an unincorporated business under Article 16-A of the Tax Law."

To the same effect, see 20 NYCRR, Section 286.1(b).

In opinion of Counsel dated July 13, 1955 (see Manual of Policy--Business Tax Article 14, Pages 1 through 4, 5/15/59) it was held that the phrase "the proportionate interest in such net income of a partner" means the distributive share of the partner in the entire net income of the joint venture rather than in that portion of the net income of the joint venture which is allocated to New York. This is in accord with the decision in the case of Cromwell et. al. v. Bates, et.al., 284 App. Div. 1001, where it was held that the partnership must include in gross income its entire distributive share received from the joint venture, irrespective of the fact that the joint venture was permitted to allocate its income.

The taxpayers contend that they are entitled to a salary credit allowance of $10,000 ($5,000 for each corporation) on each of the joint venture returns filed by them.

Section 386-e of the Tax Law permits in addition to the other deductions set forth therein a deduction on account of personal service of an individual or member of a partnership carrying on an unincorporated business, if such person be actively engaged in the conduct thereof.

In Manual of Policy, Income Tax Bureau, Business Tax Article 13 (5/15/59) in interpreting Article 13 of the Business Tax Regulations now contained in 20 NYCRR, Section 285.2, it is stated that no credit (salary) is allowable for services of a fiduciary or for a corporation or partnership which is a member of another partnership.

I am, therefore, of the opinion that the assessments should be sustained.

For the reasons stated above, I recommend that the determi-

nations of the Tax Commission in these matters be substantially in the form submitted herewith.

Solomon Sies
Hearing Officer

Marcus Schapiro
Approved

Earl McCullman
Approved

SS/kk:aw

January 12, 1967 (Feb. 3, 1967)

STATE OF NEW YORK

STATE TAX COMMISSION

IN THE MATTER OF THE APPLICATION

OF

Port Chester Electrical Const. Corp., and Carroll-Reimer Corp. individually and as co-partners d/b/a the firm name and style of:

Joint Venture--

PORT CHESTER ELECTRICAL CONST. CORP., and CARROLL-REIMER CORP.

FOR REVISION OR REFUND OF UNINCORPORATED BUSINESS TAXES UNDER ARTICLE 16-A OF THE TAX LAW FOR THE YEAR 1957.

The taxpayer herein having filed an application for revision or refund of unincorporated business taxes under Article 16-A of the Tax Law and a hearing having been held in connection therewith at the office of the State Tax Commission, 80 Centre Street, New York City, N.Y. on the 18th day of September, 1958 before Solomon Sies, Hearing Officer of the Department of Taxation and Finance, at which hearing the taxpayer was represented by Louis Wilk, Esq., 276 Fifth Avenue, New York, N.Y. and Alexander Aaron, C.P.A., appeared as witness, and the matter having been duly examined and considered,

The State Tax Commission hereby finds:

(1) That at all of the times hereinafter mentioned Port Chester Electrical Construction Corp. and Carroll-Reimer Corp. were and still are domestic corporations organized under the laws of the State of New York and engaged in the electrical contracting business; that on or about March 25, 1955 Port Chester Electrical Construction Corp. entered into a joint venture with Carroll-Reimer Corp. under an agreement in writing; that the aforementioned joint venturers also entered into a joint contract for the installment

of the electrical work at the office building for Baston Properties Corp., Harrison, New York as sub-contractors pursuant to a contract with Starrett Bros. & Eken under date of March 21, 1956; that the services rendered pursuant to the joint contract were rendered solely within the State of New York; that the activities of the joint venture constituted the carrying on of an unincorporated business pursuant to Article 16-A of the Tax Law.

(2) That the aforementioned joint venture elected to report its income for income tax purposes on a long term contract basis of accounting and reported its entire income for the year 1957, when the work was completed; that on the 1957 partnership return of the joint venture the distributive share of net income distributed to Port Chester Electrical Construction Corp. was $118,794.54 and the amount distributed to Carroll-Reisner Corp. was $79,169.69; that on its unincorporated business tax return for the year 1957 the joint venture herein claimed a 100% exemption and reported no tax due for the year 1957.

(3) That Port Chester Electrical Construction Corp. during the year 1957 carried on business both within and without the State of New York; that on the franchise tax return filed in accordance with Article 9-A of the Tax Law by Port Chester Electrical Construction Corp. for the year 1957 a business allocation percentage of .6699695 was claimed; that during 1957 Carroll-Reisner Corp. carried on business solely within the State of New York and did not claim any allocation on its franchise tax filed under Article 9-A of the Tax Law.

(4) That on May 31, 1960 the Department of Taxation and Finance made an additional assessment (Assessment No. B 7[illegible]) for the year 1957 in the amount of $1,[illegible].47 against the joint venture herein, correcting the exemption claimed pursuant to

section 386-f of the Tax Law permitting an exemption for Port Chester Electrical Construction Corp. only to the extent of $78,782.80, which is .6956% of the distributive share, from the joint venture net income, and allowed the exemption for Carroll-Haimer Corp. of $79,169.69, the entire amount received by it from the joint venture; that, in addition, a statutory exemption of $3,000 was also allowed the joint venture.

(3) That the taxpayer joint venture contends that it is entitled to partner's salary credit allowance of $3,000 for each corporation, or a total salary credit allowance of $10,000.

Based upon the foregoing findings and all of the evidence presented herein, the State Tax Commission hereby

DETERMINES:

(A) That in addition to the statutory exemption of $3000, the taxpayer joint venture was only entitled to exemptions of the amounts of the proportionate interest of the joint venturers in the joint venture net income as computed for unincorporated business tax purposes to the extent that such amounts are includible in the net income of such joint venturers allocable to this State under Article 9-A of the Tax Law in accordance with the intent and meaning of section 386-f of the Tax Law and 20 NYCRR, section 285.1(b); that accordingly only the amounts of $78,782.80 and $79,169.69 were properly allowed as exemptions.

(B) That the salary credit allowance for partners' services cannot be permitted inasmuch as both the member partners of the joint venture are corporations in accordance with the provisions of section 386-e of the Tax Law and 20 NYCRR, section 285.8.

(C) That, accordingly, the assessment (Assessment No. B-7035[illegible]) is correct; that said assessment does not include any tax or other charge which could not have been lawfully demanded and that the application for revision or refund filed by the joint venture with respect to said assessment for the year 1957

[redacted] and the same is hereby denied.

[redacted] Albany, New York on the 3rd day of March , 1967.

[redacted]

/s/ JOSEPH H. MURPHY
[redacted]

/s/ JAMES R.MACDUFF
[redacted]

/s/ WALTER MACLYN CONLON
[redacted]