

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition :  
of :  
Overseas National Airways, Inc. : AFFIDAVIT OF MAILING  
for Redetermination of a Deficiency or a Revision :  
of a Determination or a Refund of Corporation Tax :  
under Article 9 of the Tax Law for the Years :  
1968-1971 & 1974-1977. :

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State of New York  
County of Albany

Jay Vredenburg, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 22nd day of January, 1982, he served the within notice of by certified mail upon Overseas National Airways, Inc., the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Overseas National Airways, Inc.  
645 Madison Ave.  
New York, NY 10022

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) 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  
22nd day of January, 1982.

*Bernie P. Haglund*

*J. Vredenburg*

STATE OF NEW YORK  
STATE TAX COMMISSION

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In the Matter of the Petition :  
of :  
Overseas National Airways, Inc. : AFFIDAVIT OF MAILING  
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State of New York  
County of Albany

Jay Vredenburg, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 22nd day of January, 1982, he served the within notice of Decision by certified mail upon Edward H. Hein the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Edward H. Hein  
Breed, Abbott & Morgan  
Citicorp Ctr., 153 East 53rd St.  
New York, NY 10022

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) 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  
22nd day of January, 1982.

*Corrie A. Haglund*

*J. Vredenburg*

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

January 22, 1982

Overseas National Airways, Inc.  
645 Madison Ave.  
New York, NY 10022

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) 184 of the Tax Law, any proceeding in court to review an adverse decision by the State Tax Commission can only be instituted under Article 78 of the Civil Practice Laws 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  
Deputy Commissioner and Counsel  
Albany, New York 12227  
Phone # (518) 457-6240

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative  
Edward H. Hein  
Breed, Abbott & Morgan  
Citicorp Ctr., 153 East 53rd St.  
New York, NY 10022  
Taxing Bureau's Representative

STATE OF NEW YORK  
STATE TAX COMMISSION

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In the Matter of the Petition	:	
of	:	
OVERSEAS NATIONAL AIRWAYS, INC.	:	DECISION
for Redetermination of a Deficiency or for	:	
Refund of Corporation Tax under Article 9 of	:	
the Tax Law for the Years 1968 through 1971	:	
and 1974 through 1977.	:	

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Petitioner, Overseas National Airways, Inc., John F. Kennedy International Airport, Jamaica, New York 11430, now 645 Madison Avenue, New York, New York 10022, filed petitions for redetermination of a deficiency or for refund of corporation tax under Article 9 of the Tax Law for the years 1968 through 1971 and 1974 through 1977 (File No. 13977).

A formal hearing was held before Frank Romano, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York on February 25, 1979 at 1:15 P.M. and thereafter continued before Edward Goodell, Hearing Officer, at the same offices on May 19, 1980 at 9:35 A.M. Petitioner appeared by Breed, Abbot & Morgan, Esqs. (Edward F. Hein, Esq. and Judith F. Goodman, Esq., of counsel). The Audit Division appeared by Peter Crotty, Esq. (Alexander Weiss, Esq., and Ralph J. Vecchio, Esq., of counsel).

ISSUES

Whether petitioner, a Delaware corporation with its principal office in New York, whose business was the interstate and foreign transport by air of civilian and military passengers and cargo (with no flights on which passengers or cargo were transported from one point within New York to another point within New York) is subject to tax liability under section 184 of Article 9 of

the Tax Law upon the following items of its gross earnings during the periods at issue:

- a. Receipts derived from the sale of an interest in a contract for the construction of passenger cruise ships,
- b. receipts derived from the sale of rights in a jet assisted take off system ("JATO"),
- c. certain interest income,
- d. certain dividend income,
- e. receipts derived from administrative services provided to one of its subsidiaries, and
- f. fees received by the petitioner from the cancellation of charter flights.

#### FINDINGS OF FACT

1. For the 13 calendar quarters ending December 31, 1968 through December 31, 1971, the petitioner reported its liability for the taxes imposed by section 184 of the New York Tax Law ("gross earnings tax") to the Corporation Tax Bureau of the Department of Taxation and Finance for the State of New York ("Department") on forms CT-36, Report of Transportation and Transmission Corporation. Each such form together with the payment of the tax liability indicated thereon was filed in the month designated by law.

2. On December 17, 1971, the petitioner executed form CT-318, Consent Extending the Period of Limitation for the Assessment of Tax under Article 9, for the purpose of extending to March 1, 1973, the period during which the gross earnings tax might be assessed for the calendar quarters ending December 31, 1968 through June 30, 1971.

3. On January 10, 1973, petitioner executed form CT-318, Consent Extending the Period of Limitation for the Assessment of Tax under Article 9, for the purpose of extending to June 1, 1973 the period during which the gross earnings

tax might be assessed for the calendar quarters ending December 31, 1968 through December 31, 1971, which said form was subsequently executed on behalf of the New York State Tax Commission.

4. On March 15, 1973, the Department mailed to the petitioner a Notice of Deficiency regarding its liability for gross earnings tax for the 13 calendar quarters aforesaid together with statements of audit adjustment for each of said calendar quarters asserting a gross earnings tax deficiency for each of said calendar quarters, the total principal amount thereof being the sum of \$66,858.80.

5. The said statements of audit adjustment incorporated the explanation of adjustments set forth in a letter addressed to the petitioner by the Department, dated January 10, 1973, stating in part that:

"An examination of your records indicates that additional taxes are due to the State of New York as a result of gross receipts arising from or growing out of the employment of capital, whether the capital is employed in transportation or transmission or otherwise."

6. On June 13, 1973, the petitioner duly filed with the Department form CT-92, Petition for Redetermination of Deficiency, with respect to the said sum of \$66,858.80 in principal amount of tax deficiency asserted as additional gross earnings tax for the aforesaid 13 calendar quarters and any interest accruing on such deficiency.

7. Pursuant to Section 184 of Article 9 of the Tax Law, the petitioner duly filed form CT-36, entitled "Report of Transportation and Transmission Corporations and Associations Franchise Tax on Gross Earnings" for 10 quarters beginning with the quarter that ended on September 30, 1974 and for nine subsequent quarters, the last of which was the quarter for the period ended on December 31, 1977.

8. On March 23, 1979 the Audit Division issued Notices of Deficiency against the petitioner for each of the aforesaid ten quarters referred to in paragraph 7 above together with statements of audit adjustment for each of said quarters asserting an additional gross earnings tax deficiency for each of said quarters "based on the findings of a recent field audit," the aggregate principal amount thereof for said 10 quarters being the sum of \$15,204.18.

9. Petitioner timely filed a Petition for Redetermination of a Deficiency or for Refund of Corporation Tax under Article 9, of the Tax Law with respect to all 10 of the quarters described in paragraph 7 above.

10. Overseas National Airways, Inc., the petitioner in this proceeding ("ONA"), was incorporated in Delaware on July 13, 1950.

11. During the periods at issue ONA had its executive offices and corporate headquarters at John F. Kennedy International Airport, in Jamaica, New York.

12. During the periods at issue, ONA had sales offices in various cities in the United States, including New York City, and Europe with additional sales agents in other foreign locations in the Pacific and Middle East. During the periods at issue, ONA's primary maintenance facility was located in Norfolk, Virginia.

13. During the periods at issue, ONA was a supplemental air carrier authorized by the Civil Aeronautics Board and the Federal Aviation Administration to provide on a charter basis air transportation to civilian and military charterers.

During the periods at issue ONA held certificates authorizing it to provide for a consideration the following services: (a) passenger and cargo transportation on a world-wide basis for the Department of Defense, (b) civilian passenger transportation between and among the fifty United States and the

District of Columbia, (c) civilian passenger transportation between the forty-eight contiguous United States on the one hand, and Europe, Africa, and Asia as far east as India on the other hand, and (d) civilian passenger and civilian cargo transportation between the United States and the District of Columbia on the one hand and the islands in the Caribbean Sea and the Gulf of Mexico on the other hand.

14. ONA's principal business during the periods at issue was interstate and foreign air transportation of passengers and cargo.

15. ONA did not have authority to transport passengers or cargo from any airfield in New York to another airfield in New York and, during the periods at issue, did not operate any flights, civilian or military, from one point in New York State to any other point in New York State.

16. (a) On or about May 1, 1969 ONA entered into a contract in the Netherlands with De Rotterdamsche Droogdok Maatschappij N.V. ("RDM") a corporation organized and existing under the laws of the Netherlands, engaged in the business of shipbuilding, for the construction by RDM of a Cruise Passenger Vessel for the transportation of passengers on two-week cruises in tropical, subtropical and temperate waters, air conditioned throughout and, at ONA's option, to be registered under the Panamanian or Curacao flag.

(b) Said contract further provided, in part, that it "shall be governed and interpreted in accordance with the laws of the Netherlands"; that payments under the contract by ONA to RDM should be made in Dutch guilders deposited by ONA into the account of RDM with a Dutch bank at Rotterdam; that "the Vessel should be delivered afloat, at a safe berth alongside the builder's premises" in Rotterdam where its construction took place; and that ONA had the option of



ordering the construction of two additional Vessels on terms and conditions therein specified.

(c) Said contract was negotiated in Rotterdam and ONA financed the construction of the Vessel with a loan from a Dutch bank.

17. (a) On or about May 1, 1970 ONA entered into an agreement with the Cunard Steam-Ship Company Limited of London (Cunard) pursuant to which it was agreed in part that ONA and Cunard would form a private limited company to be incorporated in England, the share capital of which would be divided equally between them; that ONA would assign to it all of its rights and obligations under its aforesaid construction contract with RDM; and that said private limited company so to be incorporated in England would operate the aforesaid Vessel provided to be constructed in Rotterdam as aforesaid as a joint Venture of ONA and Cunard.

(b) Said agreement between ONA and Cunard was negotiated on the high seas and in London and was signed in the offices of Cunard in London.

(c) In accordance with the said agreement between ONA and Cunard, a private limited company, Cunard-ONA Limited was incorporated on June 4, 1970 under the laws of the United Kingdom, with its principal offices located in London and on June 14, 1970 ONA assigned to Cunard-ONA Limited "all of its titles rights and benefits under and to the Building Contract" between ONA and RDM referred to in paragraph 16 above. In consideration of said assignment Cunard-ONA Limited paid to ONA cash and notes.

(d) Pursuant to a Supplemental Agreement dated June 14, 1970, wholly negotiated in London and executed in London, ONA granted Cunard for nominal consideration an option to purchase all of ONA's shares of Cunard-ONA Limited,

which said option was exercised by Cunard later in 1970, Cunard thereby becoming the owner of all of the shares of Cunard-ONA Limited.

18. ONA realized a gain of \$6,691,875.00 upon the disposition of its stock in Cunard-ONA Limited and of its rights and obligations in the aforesaid construction contract between ONA and RDM. This gain was included in the tax base in computation of the deficiency asserted herein as aforesaid.

19. The foregoing transactions relative to the Cruise Passenger Vessel described in paragraphs 16 to 18 above were approved or ratified by the Board of Directors of ONA in New York City.

20. (a) ONA developed a program known as the "Jato Program", an acronym for "a jet assisted take-off" system, designed for installation on its DC-9 airplanes in order to enable them to take off from high elevation airports, a necessary condition for qualification under ONA's Navy and Air Force contracts.

(b) ONA's Jato Program was approved by the Federal Aviation Administration which issued to ONA a Supplemental Type Certificate, known as an "STC", the equivalent of a patent in the aviation industry.

(c) ONA, during the periods at issue, entered into a contract with McDonnell Douglas Corporation in Long Beach, California for the purchase by ONA of DC-10 airplanes and, in connection with that contract, sold to McDonnell Douglas Corporation its rights in the Jato Program.

(d) Under the terms of the said contract ONA received payment for its assignment of its rights in the Jato Program in the form of a credit by McDonnell Douglas Corporation against the purchase price of the DC-10 airplanes that ONA contracted to purchase as aforesaid.

21. ONA realized a gain of \$299,555.00 on the assignment of its rights in the Jato Program as aforesaid which said gain was included in the tax base in computation of the deficiency asserted herein.

22. Included in the tax base in computation of the deficiency asserted herein was interest earned by ONA during the periods at issue totaling \$1,279,273.00 derived by ONA from the following transactions outside New York:

- a. Progress payments that ONA was required to make in advance to McDonnell Douglas Corporation in connection with its manufacture of aircraft for ONA, interest being earned on such deposits by ONA at a specified contractual rate, which along with actual payments was credited at the time of purchase toward the total purchase price of said aircraft.
- b. Security deposits that ONA was required to make in connection with DC-8 airplanes leased to ONA by the CIT Corporation and a DC-8 leased to ONA by GATX Corporation.
- c. Promissory notes delivered to ONA by Flying Tigers Corporation as part of the purchase price in connection with its purchase from ONA of a DC-8 airplane.
- d. Promissory notes delivered to ONA as part of its sale of the shares of stock of International Travel Club of California.
- e. Compensating balance deposited by ONA in connection with loans made to ONA by a consortium of banks which financed aircraft acquisitions.
- f. Deposits from charterers of ONA's aircraft.

23. Also included in the tax base in computation of the deficiency asserted herein was the sum of \$652,446.00 representing interest on advances to Great Ocean Cruise Lines ("GOCL"), a Delaware corporation, under the following circumstances:

- a. GOCL was a wholly-owned subsidiary of ONA organized for the purpose of building and operating the Mississippi Queen, a paddle-wheel steamboat, as an overnight cruise ship on the Mississippi and Ohio rivers.
- b. ONA made loans to GOCL to finance the construction of the Mississippi Queen.

c. ONA was not paid interest on the aforesaid loans to GOCL but was required by the Civil Aeronautics Board to report interest expense, whether paid or accrued, as part of its rate-making requirements.

24. ONA sold all of its GOCL stock to Coca-Cola Bottling Company of New York (which is headquartered in New Jersey) and, in consideration thereof, received Coca-Cola stock and derived therefrom dividend income in the sum of \$39,196.00. Said dividend was included in the tax base in computation of the deficiency asserted herein.

25. Automated Terminal Services Incorporated, a Delaware corporation and a wholly-owned subsidiary of ONA, operated terminals at about 21 Navy bases in various parts of the United States, none of which were located within New York State. ONA provided administrative and booking services to its said subsidiary, which said services were rendered in connection with ONA's air transportation business and for which ONA was paid by its said subsidiary.

26. ONA received management income from Automated Terminal Services Incorporated amounting to \$75,000.00 which said income was included in the tax base in computing the deficiency asserted herein.

27. ONA collected charter cancellation fees totaling \$53,307.00 in cases where the charterer could not fulfill the terms of its contracts. These fees were collected in the course of ONA's interstate and international air transportation business and were included in the tax base in computation of the deficiency asserted herein.

#### CONCLUSIONS OF LAW

A. That section 184 of Article 9 imposes upon transportation and transmission corporations and associations an additional franchise tax equal to a prescribed percentage of the corporation's "gross earnings from all sources within this state, excluding earnings derived from business of an interstate character,"

for the privilege of exercising its corporate franchise or carrying on its business in such corporate capacity in New York.

The Third Department, in interpreting the predecessor of section 184, held as follows:

"By gross earnings, it seems to me, that the statute means all receipts arising from or growing out of the employment of its capital, whether that capital is employed in the transportation and transmission business or otherwise." New York Central & H.R.R.R. Co. v. Roberts, 32 A.D. 113, 115 (1898).

B. That the gain from the sale of the ship contract rights, the gain from the sale of petitioner's rights in the Jato program, the dividend income, the fees from cancellation of charter flights and interest received on certain progress payments, notes and security deposits constituted income taxable under section 184.

The intangible assets, contracts, passbooks and other instruments, which were the sources of such income, were held, managed and controlled by petitioner's New York headquarters, its commercial domicile. Such intangibles had a situs in New York (Burke v. Wells, 184 N.Y. 275, affd. 208 U.S. 14 (1908); Edison Electric Light Co. v. Campbell, 138 N.Y. 543 (1893)) and were assets employed in petitioner's business in this state.

Petitioner contends that the state of commercial domicile may not levy an unapportioned tax on income from intangibles but has failed to produce any proof that it has been subjected to multiple taxation, the very offense against which the rule of apportionment is designed to protect. See Exxon Corp. v. Department of Revenue, 447 U.S. 207 (1980); Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980).

C. That the receipts from performance of administrative services for a subsidiary, which services presumably were performed in this state, were taxable under section 184.

D. That the intangibles in question were sufficiently separable from petitioner's interstate and foreign transportation business that income therefrom did not fall within the exclusion of section 184 for "earnings derived from business of an interstate character". On the other hand, transportation receipts were considered by the Audit Division as falling within such exclusion and were not subject to tax.

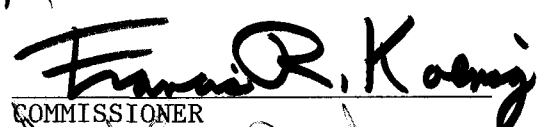
E. That the petition of Overseas National Airways, Inc. is hereby denied and the notices of deficiency issued March 15, 1973 and March 23, 1979 are sustained in full.

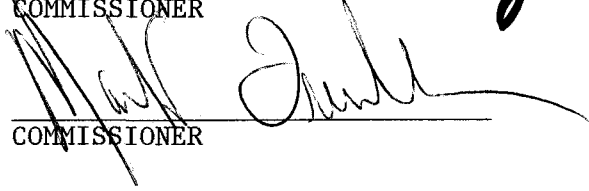
DATED: Albany, New York

JAN 22 1982

STATE TAX COMMISSION

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER