

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-00(6)C
Corporation Tax
March 29, 2000

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C000217A

On February 17, 2000, a Petition for Advisory Opinion was received from Country Knolls Water Works, Inc., 5 Municipal Plaza, Clifton Park, New York 12065.

The issue raised by Petitioner, Country Knolls Water Works, Inc., is whether it is subject to either the New York State franchise tax under Article 9-A or section 186 of Article 9 of the Tax Law, or excise tax under section 186-a of Article 9 of the Tax Law, since it is a membership corporation whose sole member is the Town of Clifton Park Water Authority, a public benefit corporation.

Petitioner submits the following facts as the basis for this Advisory Opinion.

The Town of Clifton Park Water Authority (the "Authority") was created under Title 6-B of Article 5 of the Public Authorities Law, pursuant to Chapter 724 of the Laws of 1990, approved and effective July 22, 1990 (the "Act"). The Act requires that the creation of the Authority be subject to a mandatory referendum and an affirmative vote of a majority of the voters casting ballots in the Town of Clifton Park (the "Town") referendum. On October 16, 1990, a referendum was held in the Town in accordance with the Act. Upon the affirmative vote of a two-thirds majority of the voters casting ballots in said referendum, the Authority was created as a public corporation, and its existence shall continue until terminated by law. Also, pursuant to the Act, a district (the "District") was created which embraces all the territory located within the Town that is not located within the boundaries of an existing municipal water district on the western side of the Town.

The Authority is empowered to provide water supply in the District. Under the Act, it may acquire water supply facilities and is specifically authorized to acquire all of the stock of any existing water corporation. The Authority also has the power of condemnation.

Petitioner was incorporated in 1964 under the Transportation Corporation Law. In 1995, the Authority acquired all of the stock of Petitioner, and Petitioner was reincorporated under section 1411(h) of the Not-For-Profit Corporation Law (the "NFPCL"), changing from a taxable stock corporation to a not-for-profit membership organization, with the Authority as the sole member.

Petitioner's Certificate of Reincorporation, in 1995, provides that:

- Petitioner is a local development corporation pursuant to section 1411 of the NFPCL.
- The exclusive purpose of Petitioner is to lessen the burdens of government and to act in the public interest in the portions of Clifton Park and Malta in which Petitioner lawfully

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operates. Such purpose includes, but is not limited to, entering into, from time to time, any agreement or agreements with the Authority in order to assist the Authority in carrying out its governmental purposes under the Act.

- Petitioner is a Type C corporation under section 201 of the NFPCL.
- Petitioner may do any other act or thing incidental to or connected with its purpose or in advancement thereof, but not for the pecuniary profit or financial gain of its members, directors or officers.
- All income and earnings of Petitioner shall be used exclusively for its corporate purposes or accrue and be paid to the New York Job Development Authority.
- No part of the income or earnings of Petitioner shall inure to the benefit or profit of, nor shall any distribution of its property or assets be made to any member or private person, corporate, or individual, or any other private interest.

Pursuant to a lease agreement, the Authority operates all of the assets of Petitioner as a combined water system. All of Petitioner's facilities and assets are operated by Authority employees. The Authority does not have any management or operating agreements with private entities involving assets of Petitioner. All capital improvements are owned by the Authority. The water system serves approximately 9,500 separate accounts, of which over 98 percent are residential and less than two percent are commercial, industrial and institutional. The service area of the Authority includes approximately 18.2 square miles in the Town with an additional 1.2 square miles in the towns of Malta and Halfmoon, including a total population of approximately 35,000.

The Act provides that neither the New York State Public Service Commission ("PSC") nor any other board or commission of like character has jurisdiction over the Authority in the management and control of its properties or operations or any power over the regulation of rates fixed or charges collected by the Authority.

Petitioner indicates that the Authority is not required to pay any taxes, special ad valorem levies or special assessments upon any property owned by it or under its jurisdiction, control or supervision or upon its activities, or any filing, recording or transfer fees or taxes in relation to instruments filed, recorded or transferred by it or on its behalf, provided, however, that any real property owned or under the jurisdiction, supervision or control of the Authority outside the District shall be exempt from real property taxes, ad valorem levies or special assessments only pursuant to and to the extent provided by an agreement with the governing body of the municipality in which said real property is located.

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The governing body of the Authority consists of a Board of five members, all of whom are appointed by the Town Board and who must be residents of the Town. The members of the governing board of the Authority are also the five members on the board of directors of Petitioner.

Discussion

Section 209.1 of Article 9-A of the Tax Law imposes an annual franchise tax on domestic or foreign corporations for the privilege of exercising a corporate franchise, doing business, employing capital, owning or leasing property in a corporate or organized capacity, or maintaining an office in New York State. Section 209.4 of the Tax Law, provides that a corporation liable for tax under section 186 of Article 9 of the Tax Law is not subject to tax under Article 9-A of the Tax Law.

To determine the classification and proper taxability of a corporation under either Article 9-A or section 186 of Article 9, an examination of the nature of the corporation's activities is necessary, regardless of the purposes for which the corporation was organized. See Matter of McAllister Bros., Inc. v Bates, 272 AD 511, 517. Ordinarily, a corporation is deemed to be principally engaged in the activity from which more than 50 percent of its receipts are derived. See, e.g., Re Joseph Bucciero Contracting Inc., Adv Op St Tax Commn, July 23, 1981, TSB-A-81(5)C.

Section 186 of the Tax Law imposes a franchise tax upon every corporation, joint-stock company or association formed for or principally engaged in the business of supplying water when delivered through mains or pipes, for the privilege of exercising its corporate franchise or carrying on its business in such corporate or organized capacity in this state.

Section 186-a of the Tax Law imposes an excise tax on the furnishing of utility services that is equal to three and one-quarter percent from October 1, 1998 through December 31, 1999 (three and one-half percent prior to October 1, 1998 and two and one-half percent on and after January 1, 2000) of the gross income of a utility that is subject to the supervision of the PSC or the gross operating income of every other utility doing business in New York State. For purposes of section 186-a, a "utility" includes a person subject to the supervision of the PSC and every person (whether or not such person is subject to such supervision) who sells water delivered through mains or pipes or furnishes water service by means of mains, or pipes, regardless of whether such activities are the main business of such person or are only incidental thereto. The word "person" is defined in section 186-a.2(b) of the Tax Law and includes corporations, companies, associations, joint-stock companies or associations, partnerships and LLCs. The tax imposed under section 186-a of the Tax Law is imposed in addition to the franchise tax imposed under Article 9-A or under section 186 of Article 9 of the Tax Law.

In Consolidated Edison Company of New York, Adv Op Comm T&F, December 1, 1986, TSB-A-86(22)C, the petitioner leased to the City of New York Public Utility Service ("Utility") an

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undivided interest in petitioner's electric distribution system, to the extent required for the Utility to sell and distribute preference power (electricity) to certain consumers. The petitioner retained exclusive control of its entire system. It was held that for purposes of section 186 and 186-a of the Tax Law, the Public Utility Service, as a municipality, was not a corporation subject to tax. Also, the opinion stated that "[t]he attribute that distinguishes a rental from a service is that in a rental situation that lessee has possession and efficient control of the rented equipment or rented real property. Since Con Edison has exclusive control of its entire distribution system, including all matters relating to the design, construction, expansion, operation, use maintenance and retirement of the system, Con Edison's lease to Utility of an undivided interest in Con Edison's distribution system, to the extent required to sell and distribute preference power to consumers, is not a rental but rather a service being performed by Con Edison." It was held that the petitioner's receipts from such services constituted income for services performed which was included in Petitioner's gross earnings for purposes of section 186 of the Tax Law. For purposes of section 186-a of the Tax Law, it was held that the Petitioner's receipts for such services were for services rendered that were incidental to the conduct of the petitioner's principal business, and that those receipts were taxable on the profits derived therefrom.

Section 1411(i) of the NFPCL provides that corporations reincorporated under section 1411 shall be organized and operated exclusively for the purposes set forth in section 1411(a), and that in so far as the provisions of section 1411 are inconsistent with the provisions of any other law, general or special, the provisions of section 1411 shall be controlling as to corporations reincorporated thereunder.

Section 1411(a) of the NFPCL provides that a corporation may be reincorporated under such section as a not-for-profit local development corporation operated for the exclusive public purpose of lessening the burdens of government and acting in the public interest, and in the carrying out of such purpose, the corporation will be performing an essential governmental function.

Section 1411(f) of the NFPCL provides that the income and operations of corporations incorporated and reincorporated under section 1411 shall be exempt from taxation.

In this case, Petitioner's facilities and assets consist of a water system. However, Petitioner's activities, as distinguished from Con Edison, supra, consist of the leasing of all of its facilities and assets to the Authority, pursuant to a lease agreement with the Authority, whereby Petitioner relinquished its possession and control of the facilities and assets to the Authority. Any capital improvements made are owned by the Authority. As empowered under the Act, the Authority's employees operate the facilities and assets as a combined water system in providing the water supply in the District. Under these circumstances, it is the Authority, not Petitioner, that is supplying water in the District. Therefore, Petitioner is not supplying water pursuant to section 186 of the Tax Law, and it is not subject to the franchise tax imposed under such section 186. Further, Petitioner is not

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selling water or furnishing water service pursuant to section 186-a of the Tax Law, and is not subject to the excise tax imposed under such section 186-a.

Since Petitioner is not subject to the franchise tax imposed under section 186 of the Tax Law, Petitioner would be subject to the franchise tax imposed on general business corporations under Article 9-A of the Tax Law pursuant to sections 209.1 and 209.4 of the Tax Law. However, in 1995 Petitioner was reincorporated as a not-for-profit local development corporation pursuant to section 1411 of the NFPCL with its exclusive purpose to lessen the burdens of government and act in the public interest. Accordingly, pursuant to section 1411(f) and (i) of the NFPCL, Petitioner is not subject to the franchise tax imposed under Article 9-A of the Tax Law.

DATED: March 29, 2000

/s/
John W. Bartlett
Deputy Director
Technical Services Division

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.