

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-95 (16) C
Corporation Tax
September 6, 1995

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C950502C

On May 2, 1995, a Petition for Advisory Opinion was received from Lumbermens Mutual Casualty Company, American Motorists Insurance Company, and American Manufacturers Mutual Insurance Company, c/o Paul Ferraro, Kemper National Accounting Department, B-7, 1 Kemper Drive, Long Grove, Illinois 60049.

The issue raised by Petitioners, Lumbermens Mutual Casualty Company, American Motorists Insurance Company, and American Manufacturers Mutual Insurance Company, is whether Petitioners are required to make the addition to entire net income that is otherwise required by section 1503(b)(11) of Article 33 of the Tax Law for taxable years ending after December 31, 1992 and before December 31, 1996.

Petitioners are casualty insurance companies doing business in New York State since at least January 1, 1988. Petitioners are "insurance corporations" within the meaning of section 1500(a) of Article 33 of the Tax Law and are required to pay, annually, the taxes imposed by sections 1501 and 1510 of the Tax Law.

Petitioners state that they timely filed their insurance corporation franchise tax returns for all periods ending December 31, 1988 through December 31, 1992. During each of those years, Petitioners also state that they were permitted by section 847(1) of the Internal Revenue Code ("IRC") to reduce their Federal taxable incomes by a special deduction for certain estimated tax payments and that Petitioners did so reduce their Federal taxable incomes. Those Federal special deductions are to be reversed in future periods as required by section 847(5) and (6) of the IRC. However, Petitioners state that not all Petitioners took the special deduction permitted by section 847(1) of the IRC in every period.

Petitioners state that in preparing their New York State franchise tax returns for taxable year 1988, they eliminated the special deduction permitted by section 847(1) of the IRC from their computations of their entire net incomes. Petitioners further state that they also eliminated the special deduction permitted by section 847(1) of the IRC from their computations of their entire net incomes for taxable years 1989 through 1992. Therefore, the Petitioners state that they never received the benefit of the section 847(1) of the IRC deduction in computing their entire net incomes for taxable years 1988 through 1992.

Section 1503(a) of the Tax Law provides that the entire net income of a taxpayer that is a casualty insurance company shall be its total net income from all sources which shall be presumably the same as the taxable income, but not alternative minimum taxable income, which the taxpayer is required to report to the United States Treasury Department, for the taxable year, except as provided by section 1503 of the Tax Law.

Section 1503(b)(1)(P) of the Tax Law, added by Chapter 57 of the Laws of 1993 (applicable to taxable years beginning on or after January 1, 1993), provides that entire net income shall not include the amount included in federal gross income pursuant to sections 847(5) and (6) of the IRC.

Section 1503(b)(2)(S) of the Tax Law, added by Chapter 57 of the Laws of 1993 (applicable to taxable years beginning on or after January 1, 1993), provides that entire net income shall be determined without the amount of the deduction claimed by the taxpayer pursuant to the provisions of section 847(1) of the IRC.

Section 1503(b)(11) of the Tax Law, added by Chapter 57 of the Laws of 1993 (applicable to taxable years beginning on or after January 1, 1993), provides that:

(A) Notwithstanding the provisions of [section 1503(b)(1)(P)] for taxable years beginning after [December 31, 1992] and ending before [December 31, 1996], entire net income shall include the amount determined under subparagraph (B) of this paragraph. This amount shall be included in entire net income only if the taxpayer claimed the deduction allowed by [section 847(1) of the IRC] in any taxable year beginning after [December 31, 1987] and ending before [January 1, 1993].

(B) The amount to be included in entire net income under this paragraph shall be determined as follows. The taxpayer shall calculate the total amount that will be required to be included in federal gross income pursuant to the provisions of [section 847(5) and (6) of the IRC] for federal taxable years beginning after [December 31, 1992] as a result of the deduction claimed by the taxpayer in federal taxable years beginning after [December 31, 1987] and before [January 1, 1993] pursuant to the provisions of [section 847(1) of the IRC]. The taxpayer shall divide such total amount by three. An amount equal to the resulting quotient shall be included in entire net income in each of the taxpayer's first three taxable years beginning on or after [January 1, 1993].

Chapter 57 of the Laws of 1993 amended section 1503 of the Tax Law by adding sections 1503(b)(1)(P), 1503(b)(2)(S) and 1503(b)(11) of the Tax Law. Such provisions were added to the Tax Law "to close a loophole in existing [Article 33 of the Tax Law] as it applies to property and casualty insurance corporations by uncoupling for taxable years beginning on or after January 1, 1993, from the deductions and inclusions in gross income provided for by section 847 of the [IRC]" (NY Legis Ann, 1993, p 37, 43). Such legislation codifies the position taken in American International Group, Inc., Adv Op Comm T & F, October 2, 1992, TSB-A-92(13)C, which explains that the provisions of section 847 of the IRC were not designed to create a tax benefit. The section 847 deduction was designed to remedy a financial accounting and reporting concern of insurers who must discount their unpaid loss reserves. The tax liability of each insurer and the cash flow to the Department of Treasury is the same whether or not the deduction is claimed (except for the possibility of a non-interest bearing refund in the 16th year after payment). Therefore, the Advisory Opinion states that in order to properly reflect entire net income for purposes of Article 33 of the Tax Law, it is necessary to disallow the special deduction set forth in section 847 of the IRC in the year or period such deduction is claimed for Federal income tax purposes. The Advisory Opinion also states that, in order to properly reflect entire net income in subsequent taxable years, it is necessary for the taxpayer to exclude from entire net income, the amount of reduction to the special loss discount account [set up pursuant to section 847 of the IRC] which is included, pursuant to sections 847(5) and (6) of the IRC, in gross income for Federal income tax purposes in such subsequent taxable years.

A casualty insurance company computes its entire net income under section 1503 of the Tax Law by starting with Federal taxable income and making the modifications and adjustments contained in section 1503 of the Tax Law.

Sections 1503(b)(1)(P) and 1503(b)(2)(S) of the Tax Law provide for the uncoupling, for purposes of Article 33 of the Tax Law, from the Federal provisions contained in section 847 of the IRC applicable to taxable years beginning on or after January 1, 1993. The add back required by section 1503(b)(11) of the Tax Law is necessary to uncouple, for purposes of Article 33 of the Tax Law, from the special deduction set forth in section 847(1) of the IRC that a taxpayer claimed when computing Federal taxable income in any taxable year beginning after December 31, 1987 and ending before January 1, 1993. The taxpayer is required to include in entire net income the total amount that will be required to be included in Federal gross income pursuant to the provisions of section 847(5) and (6) of the IRC for Federal taxable years beginning after December 31, 1992 as a result of such special deduction claimed, pursuant to section 847(1) of the IRC, by the taxpayer in Federal taxable years beginning after December 31, 1987 and before January 1, 1993. The taxpayer shall include one-third of this amount in entire net income for each of the taxpayer's first three taxable years beginning on or after January 1, 1993.

Herein, Petitioners claimed the special deduction set forth in section 847(1) of the IRC when computing their Federal taxable incomes for taxable years beginning after December 31, 1987 and ending before January 1, 1993. Note that not all of the Petitioners claimed the special deduction for every taxable year. However, for the taxable years that the Petitioners claimed such special deduction when computing their Federal taxable incomes, such Petitioners added back such deductions when computing their entire net incomes under section 1503 of article 33 of the Tax Law for such taxable years.

Accordingly, since the purpose of the add back required by section 1503(b)(11) of the Tax Law is to uncouple for purposes of Article 33 of the Tax Law, from the section 847 of the IRC provisions for taxable years 1988 through 1992, that provision is inapplicable to Petitioners who claimed the special deduction set forth in such section 847(1) of the IRC when computing their Federal taxable incomes for taxable years beginning after December 31, 1987 and ending before January 1, 1993, but who already "uncoupled" from such provisions by having added back such special deductions when computing their entire net incomes under section 1503 of Article 33 of the Tax Law for such taxable years.

DATED: September 6, 1995

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

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