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

TSB-A-95 (4) I
Income Tax
March 15, 1995

STATE OF NEW YORK

COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. I941110C

On November 10, 1994, a Petition for Advisory Opinion was received from Jeffrey J. Pirruccello, McGrath, North, Mullin & Kratz, 222 South 15th Street, Suite 1400, Omaha, Nebraska 68102.

The issue raised by Petitioner, Jeffrey J. Pirruccello, is whether interest income, which is derived from a limited liability company and distributed to its individual members who do not reside or have nexus in New York State, is subject to New York State personal income tax under Article 22 of the Tax Law.

A limited liability company (the "Company") is considering locating its principal place of business in New York State. The Company is a limited liability company organized under the laws of Iowa. Parent ("Parent"), a multi-state business, indirectly owns all of the common interests in the Company through two wholly-owned subsidiaries, both of which are corporations organized in a jurisdiction other than New York (the "Subsidiaries"). Preferred interests in the Company are held by various parties unrelated to Parent who are located both within and without New York. The holders of preferred interests have no right to manage the Company.

The Company exists solely for the purpose of issuing preferred and common membership interests ("securities") and lending the proceeds from the issuance to Parent. Thus, the Company is simply a passive investment vehicle. The Company currently holds four notes due from Parent. The interest paid by Parent to the Company is distributed to the Company's members based upon each member's proportionate interest in the Company.

The entity acting as the securities depository for the preferred securities is located in New York. The books and records related to the Company and the Subsidiaries will be kept in New York. The principal office and mailing address of the Company and the Subsidiaries will be in New York. The company will engage in no other activity except as needed to collect the four notes and to administer this investment for the benefit of its members. Certain officers of the Company and the Subsidiaries as well as the directors of the Subsidiaries will reside in New York. Further, the Company and the Subsidiaries will qualify to do business in New York.

This advisory opinion assumes that the Company is a limited liability company that is treated as a partnership for Federal income tax purposes.

Section 601(f) of the Tax Law states:

> A partnership as such shall not be subject to tax under [Article 22]. Persons carrying on business as partners shall be liable for

> tax under [Article 22] only in their separate or individual capacities. As used in [Article 22], the term "partnership" shall include, unless a different meaning is clearly required, a subchapter K limited liability company. The term "subchapter K limited liability company" shall mean a limited liability company classified as a partnership for federal income tax purposes. The term "limited liability company" means a domestic limited liability company or a foreign limited liability company, as defined in section one hundred two of the limited liability company law.

Section 601(e) of the Tax Law imposes a personal income tax for each taxable year on a nonresident individual's taxable income which is derived from sources in New York State. The tax is equal to the tax computed as if the individual were a resident, reduced by certain credits and multiplied by the New York source fraction, the numerator of which is the individual's New York source income and the denominator of which is the individual's New York adjusted gross income.

Section 632(a)(1) of the Tax Law provides, in pertinent part, that

[i]n determining New York source income of a nonresident partner of any partnership, there shall be included only the portion derived from or connected with New York sources of such partner's distributive share of items of partnership income, gain, loss and deduction entering into his federal adjusted gross income, as such portion shall be determined under regulations of the [Commissioner of Taxation and Finance] consistent with the applicable rules of section six hundred thirty-one.

Section 631(b)(2) of the Tax Law states that in determining the New York source income of a nonresident individual, "[i]ncome from intangible personal property, including annuities, dividends, interest, and gains from the disposition of intangible personal property, shall constitute income derived from New York sources only to the extent that such income is from property employed in a business, trade, profession, or occupation carried on in this state."

It is established that the passive holding of investments by a nonresident is not the employment of property in a business, trade, profession or occupation carried on in New York State. In Delmhorst v State Tax Com'n, (1983) 92 AD2d 981, aff'd 60 NY2d 628, it was held that since the income producing intangible personal property was an installment note, upon which interest was paid, and not the stock exchange seat covered by the note, and since the installment note was never used in a business, trade, or profession or occupation carried on in New York as required under applicable tax provisions, the interest income received from the installment note by the taxpayers for the years in which they were nonresidents was not taxable as New York income. Also, in Katz v State Tax Com'n, (1985) 110 AD2d 1029, it was held that nonresidents' interest income from unsecured installment notes arising out of the sale of real property was not taxable, as the notes themselves were never used in a New York trade or business.

In general, the rules for determining whether or not an item of income is derived from or connected with New York sources are no different for nonresident partners than for other nonresident taxpayers. Thus, in accordance with section 632(a)(1) of the Tax Law, if an item of income would not be derived from or connected with New York sources for a nonresident individual then such item of income would not be considered to be derived from or connected with New York sources for a nonresident partner. See, E. Parker Brown II, Adv Op Comm T & F, January 3, 1990, TSB-A-90(1)I.

Under the facts as set forth herein, if the interest payments on the notes had been received by a nonresident individual, such interest income would not be

considered income derived from or connected with New York sources within the meaning and intent of section 632(a)(1) of the Tax Law. Therefore, where such interest payments are received by a nonresident partner they must be accorded the same treatment; that is, such interest income is not considered to be derived from or connected with New York sources.

Pursuant to section 601(e)and 632(a)(1) of the Tax Law, if the Company is a limited liability company classified as a partnership for Federal income tax purposes, the interest paid by Parent to the Company, on the notes held by the Company that is distributed by the Company to an individual who is a member of the Company, is interest income of the individual that is not considered to be derived from or connected with New York sources. Accordingly, if such individual member of the Company is a nonresident of New York State and has no other New York source income for the taxable year, such nonresident individual is not subject to personal income tax in New York State.

DATED: March 15, 1995

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

NOTE: The opinions expressed in Advisory 0pinions are limited to the facts set forth therein.