

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

TSB-A-92 (18) C
Corporation Tax
December 16, 1992

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C920924A

On September 24, 1992, a Petition for Advisory Opinion was received from Housing Authority Risk Retention Group, Inc., 677 South Main Street, Cheshire, Connecticut 06410.

The issue raised by Petitioner, Housing Authority Risk Retention Group, Inc., is whether it is exempt from franchise taxes on insurance corporations under Article 33 of the Tax Law as a state instrumentality.

Petitioner is a nonprofit, nonstock corporation. Petitioner was formed for the purpose of providing its members the opportunity to pool certain liability risks. Membership in Petitioner is limited to individual public housing authorities, public housing and development or redevelopment authorities, and similar authorities or boards operated for the primary purpose of providing public housing for low-income persons, created and existing as political subdivisions of any state or the District of Columbia, or possession of the United States or an agency thereof. The liabilities covered will be connected with properties actually owned by the member authorities or a liability arising out of a member's duty to inspect certain privately owned lower income development properties. In all events, no liability of any one other than a member authority will be covered.

Petitioner will be governed by a board of directors, consisting of not less than three and not more than 21 persons, elected by the member representatives at the annual meeting. Each member housing authority shall appoint one individual to serve as its representative to Petitioner. The individual must be an employee or an elected or appointed official of a member housing authority.

The board of directors will determine the annual premiums, based on each member authority's rating category, which takes into account its loss history, deductible level, coverage ceiling, and related factors. The board has the authority to assess retroactive premiums if deemed necessary to cover the losses of the group.

In addition to the annual premiums, members are required to make an initial surplus contribution in order to provide reserves for potential claims. The amount of the initial surplus contribution has been set at fifty percent of each authority's initial annual premium. Additional contributions may be required of all member authorities to cover unexpected losses or other expenses.

To the extent that Petitioner has excess income at the end of a fiscal year which is not necessary to meet current losses and expenses of Petitioner, such income will either be added to the reserves in order to provide additional investment income and reduce the amount of surplus contributions or premium payments which would otherwise be required of member authorities, or distributed to member authorities in the form of dividends.

Each member of Petitioner shall agree to continue membership for not less than three years, unless it is forced out by the occurrence of certain events. If a member is forced out, it will be entitled to receive a refund of all of its account. If a member withdraws during the three year period for any other reason, the board reserves the right to withhold the member's account in full. At the conclusion of such period, a member may withdraw for any reason and Petitioner will refund to that member that percentage of those cumulative reserve fund contributions made to Petitioner by the withdrawing member according to a prescribed schedule. Upon dissolution of Petitioner and after payment of all liabilities, the remaining assets shall be distributed among the members based on the annual premiums.

Section 1 of the New York State Public Authorities Law provides that a public authority, is an agency and instrumentality of the State. Section 15 of the New York State Public Housing and Urban Renewal Law provides that a municipal housing authority is an agency and instrumentality of the State.

Section 115 of the Internal Revenue Code (hereinafter "IRC") provides that gross income does not include income derived from the exercise of an essential governmental function and accruing to a state or political subdivision of a state or income accruing to the government of any possession of the United States, or any political subdivision thereof.

In Rev Rul 90-74, 1990-2 CB 34, it is held that the income of an organization formed, operated, and funded by political subdivisions to pool their casualty risks is excluded from gross income under section 115(1) of the IRC. Similarly, the income of an organization formed, operated, and funded by one or more political subdivisions (or by a state and one or more political subdivisions) to pool their risks in lieu of purchasing insurance to cover their public liability, workers' compensation, or employees' health obligations is also excluded under section 115(1) of the IRC if private interests do not, except for incidental benefits to employees of the participating state and political subdivisions, participate in or benefit from the organization.

Petitioner received a letter ruling from the Internal Revenue Service dated January 5, 1988 stating that the income of Petitioner is excludable from gross income under section 115 of the IRC. The ruling's basis is that the provision of financial protection against losses by Petitioner is an enterprise that is desirable from the standpoint of the governmental entities because use of Petitioner fulfills the need of the governmental entities to provide this type of protection at a cost lower than could be obtained commercially. Participation of the governmental entities in Petitioner is an activity within the function of a sovereign to conduct because the governmental entities must take steps to protect their financial security with liability protection. Thus, Petitioner is performing an essential governmental function that is within the scope of section 115 of the IRC.

Also, the letter ruling states that with respect to the income accruing requirement in section 115 of the IRC, the income of Petitioner will be used for the provision of liability protection or the payment of claims or will be returned to the participating public authorities. Upon dissolution of Petitioner and after the satisfaction of all the obligations of Petitioner, the participating governmental

entities are entitled to a return of the remaining agency assets in proportion to their participation in the agency. Accordingly, the arrangement satisfies the accruing requirement of section 115 of the IRC.

Section 1512(a)(1) of the Tax Law provides that the Franchise Taxes on Insurance Corporations does not apply to "the government of the United States, or of any state or municipality thereof, or any instrumentality of any such government".

Herein, Petitioner is an "instrumentality" within the meaning of section 1512(a)(1) of the Tax Law and is therefore exempt from New York State franchise taxes on insurance corporations pursuant to section 1512(a)(1) of the Tax Law.

DATED: December 16, 1992

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

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