

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

TSB-A-98(14)C  
Corporation Tax  
TSB-A-98(9)I  
Income Tax  
September 4, 1998

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. Z980601B

On June 1, 1998, a Petition for Advisory Opinion was received from H.O. Wolding, Inc., P.O. Box 56, Nelsonville, Wisconsin 54458.

The issues raised by Petitioner, H.O. Wolding, Inc., are (1) how to compute the taxable income for a short period as a Subchapter S corporation under Article 9-A of the Tax Law where the corporation was previously an Article 9 taxpayer, and (2) how this change in status from an Article 9 taxpayer to an Article 9-A S corporation affects the nonresident shareholders for purposes of Article 22 of the Tax Law.

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

Petitioner is an interstate motor carrier that was previously subject to tax under sections 183 and 184 of Article 9 of the Tax Law. Effective January 1, 1998, Petitioner is subject to tax under Article 9-A of the Tax Law. Petitioner has received approval to be treated as a New York State S corporation with a fiscal year ending June 30. Petitioner's first report under Article 9-A will be for a short period — January 1, 1998 through June 30, 1998.

All of Petitioner's shareholders are residents of Wisconsin, and are calendar year taxpayers for federal income tax purposes.

Discussion

Issue 1

The corporation franchise tax treatment for a New York S corporation is explained in the New York State Department of Taxation and Finance Publication 35 (2/96) New York Tax Treatment of S Corporations and their Shareholders in Parts V and VI.

Section 208.1-A of the Tax Law provides that the term "New York S corporation" means, with respect to any taxable year, a corporation subject to tax under Article 9-A of the Tax Law for which an election is in effect pursuant to section 660(a) of the Tax Law for the year.

Section 210.1(g) of the Tax Law provides that a New York S corporation is not subject to the alternative minimum tax or the capital base tax. It is only subject to the tax on the portion of its entire net income allocated within New York State at a rate reduced to the differential rate. If the tax at the differential rate is less than the fixed dollar minimum tax, the fixed dollar minimum tax applies. The differential rate is the difference between the

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corporate rate under Article 9-A and the Article 22 personal income tax equivalent rate.

Section 208.9(ii) of the Tax Law provides that the term "entire net income" means total net income from all sources, which shall be presumably the same as the entire taxable income (but not alternative minimum taxable income) which the taxpayer would have been required to report to the United States Treasury Department if it had not made an election under Subchapter S of Chapter one of the IRC, except as modified as required by section 208.9 and section 210.3(d) and (e) of the Tax Law.

Pursuant to section 208.9(ii) of the Tax Law, Petitioner's starting point for computing entire net income, even though a New York S corporation, is Petitioner's federal taxable income computed as if Petitioner had not made the election to be treated as a federal S corporation.

Section 2-1.1(a) of the Business Corporation Franchise Tax Regulations (the "Article 9-A Regulations") provides that, in most cases, the taxable year for which a franchise tax report is to be filed is the same as the taxpayer's taxable year for federal income tax purposes, or that portion of the federal taxable year for which the taxpayer is subject to tax under Article 9-A of the Tax Law.

Section 208.9(h)(1) of the Tax Law and section 3-2.9(a) of the Article 9-A Regulations provides that if the entire net income required to be reported under Article 9-A is for a period different from the period covered by the taxpayer's federal income tax return, the taxpayer's entire net income must be prorated to correspond with the period covered by the report under Article 9-A. The prorated entire net income is computed as follows:

- (1) adjust federal taxable income as required by section 208.9 and section 210.3(d) and (e) of the Tax Law, sections 3-2.3, 3-2.4, 3-2.5 and 3-2.6 of the Regulations;
- (2) divide the entire net income by the number of calendar months, or major parts thereof, covered by the return for federal income tax purposes; and
- (3) multiply the result by the number of calendar months, or major parts thereof, covered by the report under Article 9-A.

Section 3-2.9(d) of the Article 9-A Regulations provides that, if in the opinion of the Commissioner, the method described above does not properly reflect the taxpayer's entire net income for purposes of Article 9-A during the period covered by its report, the Commissioner may determine entire net income solely on the basis of the taxpayer's income during such period.

Accordingly, Petitioner computes its entire net income pursuant to section 208.9 of the Tax Law, as if it is a New York C corporation for the entire taxable year covered by its federal income tax return. If Petitioner's federal taxable

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year is different than its New York short taxable year of January 1, 1998 through June 30, 1998, Petitioner must prorate its entire net income, pursuant to section 208.9(h)(1) of the Tax Law and section 3-2.9 of the Article 9-A Regulations, for the six months that it is subject to tax under Article 9-A.

Further, the portion of Petitioner's prorated entire net income shall be allocated within New York state pursuant to section 210.3 of the Tax Law. Pursuant to section 210.3(a)(8) of the Tax Law, if Petitioner is principally engaged in a trucking business, it shall compute its business allocation percentage by dividing Petitioner's mileage within New York State during the period covered by its report by Petitioner's mileage within and without New York State during the period.

## Issue 2

The personal income tax treatment for S corporation shareholders is explained in the New York State Department of Taxation and Finance Publication 35 (2/96) New York Tax Treatment of S Corporations and their Shareholders in Parts VII, VIII and IX.

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 computed as if the individual were a resident, reduced by certain credits, and apportioned to New York 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 631(a) of the Tax Law provides that the New York source income of a nonresident individual includes (1) the net amount of items of income, gain, loss and deduction entering into the individual's federal adjusted gross income that is derived from or connected with New York sources, including the individual's pro rata share of New York S corporation income, loss and deduction, increased by reductions for taxes described in section 1366(f)(2) and (3) of the Internal Revenue Code, and (2) the portion of the modifications described in section 612(b) and (c) of the Tax Law which relate to income derived from New York sources, including any modifications attributable to the individual as a shareholder of a New York S corporation.

In determining the amount of a nonresident's New York S corporation items which are derived from or connected with New York sources, section 632(a)(2) of the Tax Law provides that the methods and rules for allocation under Article 9-A of the Tax Law shall be used. Since, under Article 9-A, Petitioner's entire net income has been both (1) prorated to correspond with the period during which Petitioner is taxable under such Article, and (2) allocated by mileage to reflect its New York activity, it is appropriate that the Article 9-A methods and rules prescribed by section 632(a)(2) for the nonresident shareholders' allocation take into account both the proration and the mileage allocation.

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Accordingly, the nonresident shareholders of Petitioner that are calendar year taxpayers will include in New York adjusted gross income their pro rata shares of Petitioner S corporation's items of income, loss and deduction that are includable in their federal adjusted gross income for the calendar year 1998. Likewise, the nonresident shareholders will include in New York source income their prorata shares of such items of income, loss and deduction which are sourced to New York. The source of such items shall be determined using both the proration and mileage allocation methodologies employed by the Petitioner under Article 9-A of the Tax Law with respect to its entire net income for its fiscal year ending June 30, 1998.

DATED: September 4, 1998

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

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