Income/Franchise:
A Closer Look at New York’s Draft Proposed Regulations under Article 9-A Business Corporation Franchise Tax: Apportionment of Receipts from Certain Services to Investment Companies and Receipts from the Sale of Advertising

Draft Proposed New York Business Corporation Franchise Tax Regulations, Subparts 4-1, 4-2 and 4-3, N.Y. Dept. of Tax. & Fin. (9/30/16). On September 30, 2016, the New York Department of Taxation and Finance (Department) released a draft document repealing New York Business Corporation Franchise Tax Regulations Subparts 4-1, 4-2, 4-3, 4-4, 4-5, 4-7, 4-8, 4-9 and 4-10, and proposing draft regulations for New York Business Corporation Franchise Tax Regulations Subparts 4-1, 4-2 and 4-3. These draft proposed regulations are intended to clarify and interpret the general rules contained in section 210-A of the New York Tax Law that are used to determine the business apportionment fraction, pursuant to the Department’s broader effort “to amend the Article 9-A Business Corporation Franchise Tax Regulations to incorporate the changes made by the corporate tax reform legislation contained in the 2014-2015 and 2015-2016 enacted New York State Budgets.” Below, the draft proposed regulations for apportioning receipts from certain services rendered to investment companies and receipts from the sale of advertising are reviewed.


Receipts from Certain Services to Investment Companies

Draft Proposed Reg. Section 4-2.12 outlines how receipts received from an investment company arising from the sale of management, administration or distribution services (collectively, "services") provided to such investment company would be included in the service provider’s apportionment factor. For purposes of New York’s apportionment statute, the term "receipts from an investment company" includes amounts received directly from an investment company as well as amounts received from the shareholders or investors in such investment company, in their capacity as such. N.Y. Tax Law Sec. 210-A.5(d)(2)(C).

- The draft proposed regulations generally define an investment company as (1) a regulated investment company (RIC), as defined in IRC Section 851, and a partnership to which IRC Section 7704(a) applies and that meets the requirements under IRC Section 851(b); or (2) an unincorporated entity, such as a limited partnership, limited liability company, or trust, that pools capital from passive investors and trades or makes investments in stocks, bonds, securities, commodities, loans or other financial assets, but that do not otherwise conduct a trade or business. Draft Prop. Reg. Sec. 4-2.12(b)(1). An investment company that invests, directly or indirectly, in real estate generally would not be considered an investment company. Id.
- Under Draft Prop. Reg. Sec. 4-2.12(a)(2)(i), the portion of New York receipts received from services rendered to an investment company is the product of the total receipts derived from such services and a fraction, where the numerator is the sum of the monthly percentages determined for each month of the investment company’s taxable year for federal income tax purposes that ends within the taxable year of the taxpayer and the denominator is the number of such monthly percentages.
- Under Draft Prop. Reg. Sec. 4-2.12(a)(2)(ii), an investment company’s “monthly percentage” generally is a fraction comprised of the number of shares of the investment company held by New York shareholders on the last day of a month over the total number of shares outstanding. Under the draft proposed regulations, if an investment company has no outstanding shares for a given month, said month will not be included in the computation. The draft proposed regulations also provide alternative definitions for “monthly percentage” for unincorporated entities that qualify as investment companies as described above.
- Under Draft Prop. Reg. Sec. 4-2.12(b)(3), management services provided by an investment company generally would include the rendering of investment advice, determining when securities should be sold or purchased on behalf of an investment company, or the selling or purchasing of securities considered to be assets of an investment company, and related activities. In the case of investment companies that are RICs, as defined in IRC Section 851, or partnerships to which IRC Section 7704(a) applies and that meet the requirements under IRC Section 851(b), as described above, management services are limited to activities performed pursuant to contracts entered into pursuant to Section 15(a) of the Investment Company Act of 1940, as amended.
- Under Draft Prop. Reg. Sec. 4-2.12(b)(4), distribution services generally would include selling shares of an investment company. If a taxpayer is engaged in the service of selling shares of an investment company, the
additional services of advertising, servicing investor accounts (including redemptions) or marketing shares of
the investment company would also qualify as distribution services.
• Under Draft Prop. Reg. Sec. 4-2.12(b)(5), administration services would include professional services such as
legal and accounting services, as well as clerical and data processing services, but only if the service provider
also sells management or distribution services to the investment company in the same taxable year.

Receipts from the Sale of Advertising

Draft Proposed Reg. Sec. 4-2.14 outlines when receipts from the sale of advertising are included in a taxpayer’s New
York receipts. Advertising receipts take into account receipts from either of the following two activities:

• Receipts from providing advertising space or time in or on a medium for dissemination to the public or part of
the public, whether such medium is for sale or for free consumption;\(^1\) or
• Receipts from providing an advertising or marketing service.\(^2\)

Under Draft Prop. Reg. Sec. 4-2.14(b), the amount of New York receipts from providing advertising space or time in or
on a medium would be determined based on the specific medium of advertising:

• Receipts from publishing advertising in newspapers or periodicals would be sourced to New York by multiplying
such receipts by a fraction, where the numerator is the number of newspapers/periodicals containing such
advertising delivered within New York and the denominator is the total number of newspapers/periodicals
containing such advertising;
• Receipts from advertising on other physical media would be sourced to New York by multiplying such receipts
by a fraction, where the numerator is the number of New York locations of such physical media and the
denominator is the total number of locations of such physical media located everywhere;
• Receipts from advertising related to physical media that is “rolling stock,” such as buses, would be sourced to
New York by multiplying such receipts by a fraction, where the numerator is the miles operated in New York
and the denominator is the total number of miles operated everywhere;
• Receipts from advertising time in radio or television broadcasts would be sourced to New York by multiplying
such receipts by a fraction, where the numerator is the number of New York listeners or viewers and the
denominator is the total number of listeners or viewers; and
• Receipts from all other advertising furnished, provided, delivered to, or accessed by the viewer or listener
through the use of wire, cable, fiber-optic, laser, microwave, radio wave, satellite or similar successor media,
or any combination thereof, would be sourced to New York by multiplying such receipts by a fraction, where
the numerator is the number of New York listeners or viewers and the denominator is the total number of
listeners or viewers everywhere.

Under Draft Prop. Reg. Sec. 4-2.14(c)(1), receipts from providing an advertising or marketing service would include
receipts such as those received for creating or implementing an advertising campaign ("ad services"). These receipts
would be sourced to New York by multiplying receipts from ad services by a fraction, whereby the numerator is the
number of intended targets in New York and the denominator is the number of intended targets everywhere. The
proper proportion of intended targets in New York to intended targets everywhere would be determined by reliance on
statistics compiled or used as part of the market research and advertising strategy developed by the taxpayer for its
customer. However, if no statistics or other data is available, a taxpayer is permitted to use other information in order
to ascertain the proper ratio of New York intended targets to everywhere targets under Draft Prop. Reg. Sec. 4-
2.14(c)(1)(i).

Under Draft Prop. Reg. Sec. 4-2.14(c)(2), in situations where a taxpayer receives a lump sum payment for both ad
services and the actual purchase of advertising space or time, the taxpayer must allocate the lump sum among each
of the types of activities based on both the costs of purchasing the advertising or marketing space or time and the

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\(^1\) Examples of such mediums include printed page space in magazines, newspapers, bulletins, phone books; the
posting of material on billboards, buildings or vehicles; the sale of time on radio or TV broadcasts; and the sale of
space on web pages.

\(^2\) Prior to New York Tax Reform in 2014, the sourcing of receipts from providing advertising and marketing services
was not specifically addressed and was categorized generally as services.
intended targets of the advertising or marketing or by some other reasonable method. Full details must be submitted with the taxpayer’s report.

Please contact us with any questions.

— Abe Teicher (New York)  
Partner  
Deloitte Tax LLP  
ateicher@deloitte.com

Don Roveto (New York)  
Partner  
Deloitte Tax LLP  
droveto@deloitte.com

Ken Jewell (Parsippany)  
Managing Director  
Deloitte Tax LLP  
kjewell@deloitte.com

Dennis O’Toole (New York)  
Managing Director  
Deloitte Tax LLP  
deotoole@deloitte.com

Mary Jo Brady (Jericho)  
Senior Manager  
Deloitte Tax LLP  
mabrady@deloitte.com

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