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Subject: Update on New York State Combined Reporting Requirements

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State and Local Tax Alert

On March 3, 2008, the New York Department of Taxation and Finance ("Department") issued TSB-M-08(2)C http://www.tax.state.ny.us/pdf/memos/corporation/m08_2c.pdf, which clarifies and replaces TSB-M-07(6)C. This memorandum does the following: (1) changes what constitutes a substantial inter-corporate asset transfer; (2) changes what items are excluded when determining whether the taxpayer has substantial inter-corporate receipts or substantial inter-corporate expenditures; and (3) provides new information relating to combined reporting for real estate investment trusts (REITs), regulated investment companies (RICs), and insurance companies subject to Article 33 of the Tax Law. The changes are effective for tax years beginning on or after January 1, 2007.

Substantial Inter-corporate Asset Transfers

In TSB-M-07(6)C, the Department issued guidance that a transfer of assets to a related corporation would satisfy the "substantial inter-corporate transactions" requirement for combined reporting if the assets transferred constituted 10% or more of the transferor's or transferee's total assets at the time of transfer.

In the current TSB, the Department has changed its guidance on this issue for asset transfers occurring after January 1, 2007. Under the current TSB, a transfer of assets to a related corporation will satisfy the substantial inter-corporate transactions requirement when 20% or more of the transferee 's gross income results directly from the transferred assets and the corporations are engaged in a unitary business. Only assets transferred to the transferee in exchange for stock or paid-in capital are taken into account for the purposes of the test. If the corporation transfers cash, the transaction is not considered an asset transfer for purposes of the substantial inter-corporate asset test. When evaluating inter-corporate asset transfers to determine if substantial inter-corporate transactions exist, dividends received will be considered in the measuring of gross income for purposes of the 20% of gross income test above.

New Combined Reporting Rules for Real Estate Investment Trusts (REITs) and Regulated Investment Companies (RICs)

According to new amendments to tax laws of 2007, REITs and RICs may be required or permitted to make a report on a combined basis. A REIT whose capital stock is substantially owned or controlled by one or more corporations that are not REITs, are required to make a combined report with those corporations. However, a combined report will not be required if all the other corporations are also REITs. Additionally, a REIT is not required to be included in a combined report under Article 9-A if over 50 percent of the capital stock of the REIT is owned by a bank holding company as defined in section 1462(f) of the Tax Law or a banking corporation subject to tax under section 1451 of the Tax Law.

A RIC whose capital stock is owned or controlled by one or more corporations that are not RICs, is required to make a combined report with those corporations. However, a combined report will not be required if all the other corporations are also RICs. Additionally, a RIC is not required to be included in a combined report if over fifty percent of the capital stock of the RIC is owned directly or indirectly by a bank holding company as defined in section 1462(f) of the Tax Law or a banking corporation subject to tax under section 1451 of the Tax Law.

A REIT or RIC required to be included in a combined report must add to federal taxable income the deduction allowed to REITs and RICs in computing entire net income. In addition, if a REIT or RIC is required to be included in a combined report, combined business and investment capital includes the business and investment capital of all corporations, including any REIT or RIC included in the combined report.