

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

TSB-A-92 (16)C
Corporation Tax
TSB-A-92 (11) I
Income Tax
December 15, 1992

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. Z921014B

On October 14, 1992, a Petition for Advisory Opinion was received from Agent Orange Settlement Fund, Kenneth R. Feinberg, Special Master, c/o U.S. District Judge Jack B. Weinstein, United States District Court Eastern District of New York, 225 Cadman Plaza East - Room 651, Brooklyn, New York 11201.

The issue raised by Petitioner, Agent Orange Settlement Fund, is whether it is subject to income tax under Article 22 of the Tax Law or franchise tax under Article 9-A of the Tax Law.

The Agent Orange litigation began in 1978, when a Vietnam veteran filed a lawsuit against the United States government and numerous chemical companies that manufactured herbicides, including "Agent Orange," that were used as defoliants in Vietnam, claiming that he had suffered injuries as a result of being exposed to Agent Orange. Vietnam veterans throughout the United States began filing similar lawsuits and all the cases were ultimately consolidated and transferred to the United States District Court for the Eastern District of New York (Brooklyn).

In 1983, the Court certified a plaintiff class, which was defined as all persons who served in the United States, New Zealand, and Australian armed forces at any time between 1961 and 1972 and who were injured while in or near Vietnam by exposure to Agent Orange or other phenoxy herbicides. The class also included the parents, spouses and children of the veterans. Although there is no way to determine the exact size of the plaintiff class, estimates are that between 2.4 and 2.9 million veterans served in Vietnam.

On May 7, 1984, the day the trial was scheduled to begin, the attorneys for the plaintiff class and the defendant chemical companies agreed to settle the case for \$180 million. The government did not participate in the settlement and ultimately all claims against the United States were dismissed.

Under the terms of the Settlement Agreement the defendants were required to deposit the settlement monies into a fund (Petitioner) to be established, maintained and administered by the Court. In accordance with the terms of the Settlement Agreement, the Court established Petitioner in 1984 and the defendant chemical companies deposited the agreed upon monies into Petitioner in 1984 and early 1985. As provided by the Settlement Agreement, the Court's authority to administer Petitioner includes the power to direct the investment of Petitioner's assets, to appoint investment advisors, to supervise and approve the disbursement of any monies to the plaintiff class and for administrative purposes and to hire and appoint persons to assist in the administrative activities necessary to disburse Petitioner. The Court appointed Kenneth R. Feinberg as Special Master to assist in implementing and administering the Court's plan for distributing Petitioner's assets and has appointed contractors to provide claims administration, accounting, and investment management services.

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The Settlement Agreement expressly provided that the settlement would not become final (and thus the case would not be dismissed) until the Court approved the settlement pursuant to Rule 23(e) of the Federal Rules of Civil Procedure and until any appeals were resolved. After holding a series of "fairness hearings" at different locations around the country, the Court issued an order approving the settlement. In re Agent Orange Product Liability Litigation, MDL No 381, 611 F Supp 1296, 1347 (EDNY 1985). Subsequently, on May 28, 1985, the Court issued an opinion setting forth guidelines for distributing the settlement funds. In re Agent Orange Product Liability Litigation, MDL No 381, 611 F Supp 1396 (EDNY 1985). Thereafter, a number of parties filed appeals with the United States Court of Appeals for the Second Circuit. On April 21, 1987, the Court of Appeals issued an opinion upholding the settlement. In re Agent Orange Product Liability Litigation, 818 F2d 145 (2d Cir 1987). A number of parties then filed petitions for certiorari in the United States Supreme Court.

The Supreme Court denied the last of the petitions for certiorari on June 30, 1988, thus ending judicial review of the settlement. At that time, the fair market value of Petitioner's assets was approximately \$240 million. As of June 30, 1992, the fair market value of Petitioner's assets totalled approximately \$153 million. The Bank of New York and Brown Brothers Harriman & Co., each of which is headquartered in New York City, provide investment advice and retain custody of Petitioner's assets.

The Special Master has received a Private Letter Ruling from the Internal Revenue Service dated May 16, 1990 stating that (1) Petitioner was established prior to the effective date of section 468B(g) of the Internal Revenue Code of 1986 (hereinafter "IRC") and (2) Petitioner is not subject to federal income tax on the income earned on the amounts deposited therein. (See Rev Rul 71-119, 1971-1 CB 163; Rev Rul 70-567, 1970-2 CB 133. CF Rev Rul 69-300, 1969-1 CB 167.) The letter ruling also held that recipients of distributions from Petitioner would not be subject to federal income tax with respect to amounts received, which amounts would be excludible from gross income as tort damages under section 104(a) of the IRC.

In Rev Rul 71-119 (1970-2 CB 133), the Internal Revenue Service held that where a corporation deposited an amount of money with a United States District Court under an agreement of compromise and settlement, the settlement fund was not "property held in trust" within the meaning of section 641(a) of the IRC of 1954. Therein, the purpose of the settlement fund was to settle claims that were asserted against the corporation in several lawsuits brought by shareholders who alleged misstatements and omissions in registration statements filed pursuant to the Securities Act of 1933 by the corporation.

Section 601 of Article 22 of the Tax Law imposes a personal income tax on the taxable income of individuals, estates and trusts. Section 607 provides, in pertinent part, that:

"Any term used in this article shall have the same meaning as when used in a comparable context in the laws of the United States relating to federal income taxes, unless a different meaning is clearly required . . ."

Since Article 22 contains no special New York definition of a trust, an entity that does not constitute a trust for federal income tax purposes would not constitute a trust for New York income tax purposes.

Accordingly, since the Internal Revenue Service has ruled, based upon Revenue Ruling 71-119, 1971-1 CB 163 and Revenue Ruling 70-157 1970-2 CB 133 that Petitioner is not a trust for federal income tax purposes and is not subject to federal income tax on its earnings, Petitioner is not treated as a trust for New York purposes. Therefore, Petitioner is not subject to tax under Article 22 of the Tax Law.

Section 209.1 of the Tax Law imposes a franchise tax on business corporations, as follows:

For the privilege of exercising its corporate franchise, or of doing business, or of employing capital, or of owning or leasing property in this state in a corporate or organized capacity, or of maintaining an office in this state, for all or any part of each of its fiscal or calendar years, every domestic or foreign corporation, except corporations specified in subdivision four of this section, shall annually pay a franchise tax

Section 208.1 of the Tax Law provides that:

The term "corporation" includes an association, within the meaning of paragraph three of subsection (a) of section seventy-seven hundred one of the internal revenue code, a joint-stock company or association, a publicly traded partnership treated as a corporation for purposes of the internal revenue code pursuant to section seventy-seven hundred four thereof and any business conducted by a trustee or trustees wherein interest or ownership is evidenced by certificate or other written instrument ...

The term "corporation" is elucidated in section 1-2.3 of the Business Corporation Franchise Tax Regulations, which provides, in part, that:

(a) The term 'corporation' means an entity created as such under the laws of the United States, any state, territory or possession thereof, the District of Columbia, or any foreign country, or any political subdivision of any of the foregoing, which provides a medium for the conducting of business and the sharing of its gains.

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(b) ... An entity conducted as a corporation is deemed to be a corporation.

. . . .

(2) A business conducted by a trustee or trustees in which interest or ownership is evidenced by certificate or other written instrument includes, but is not limited to, an association commonly referred to as a business trust or Massachusetts trust. In determining whether a trustee or trustees are conducting a business, the form of the agreement is of significance but is not controlling. The actual activities of the trustee or trustees, not their purposes and powers, will be regarded as decisive factors in determining whether a trust is subject to tax under article 9-A of the Tax Law. The mere investment of funds and the collection of income therefrom, with incidental replacement of securities and reinvestment of funds, does not constitute the conduct of a business in the case of a business conducted by a trustee or trustees.

. . . .

Herein, Petitioner is not a trust for federal income tax purposes and the activities of Petitioner do not constitute the conduct of a business as contemplated by section 208.1 of the Tax Law. Accordingly, Petitioner is not deemed a corporation within the meaning of section 208.1 of the Tax law and is not subject to franchise tax under Article 9-A of the Tax Law.

DATED: December 15, 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.