

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

| | | |
|--|---|----------------|
| In the Matter of the Petition | : | |
| of | : | |
| FIRST FORTIS LIFE INSURANCE COMPANY | : | DECISION |
| for a Redetermination of a Deficiency or for Refund of | : | DTA NO. 814613 |
| Franchise Tax on Insurance Corporations under Article 33 | : | |
| of the Tax Law for the Years 1991 and 1992. | : | |

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on June 5, 1997 with respect to the petition of First Fortis Life Insurance Company, 220 Salina Meadows Parkway, P.O. Box 3209, Syracuse, New York 13220-3209. Petitioner appeared by LeBoeuf, Lamb, Greene & MacRae, L.L.P. (Hugh T. McCormick, Esq., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Paul Lefebvre, Esq., of counsel).

The Division of Taxation filed a brief in support of its exception and a reply brief. Petitioner filed a brief in opposition. Oral argument, at the Division of Taxation's request, was heard on December 11, 1997 in New York, New York.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUE

Whether petitioner may compute the additional tax on premiums imposed under Tax Law § 1510 using the tax rates appropriate for life insurance corporations as provided for in Tax Law

§ 1510(b) or, instead, is required to use the tax rate for all other insurance corporations as provided for in Tax Law § 1510(a).

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Pursuant to section 306 of the State Administrative Procedure Act and 20 NYCRR 3000.15(d)(6), the Division of Taxation (hereinafter "Division") submitted five proposed findings of fact all of which are accepted and incorporated below.

During 1991 and 1992, petitioner was an insurance company organized under the laws of New York. During each of these years petitioner held a valid license issued by the New York State Insurance Department that allowed petitioner to write "life, annuities, and accident and health insurance, as specified in paragraphs 1, 2, and 3 of Section 1113 of the New York Insurance Law."¹ Petitioner was a "member insurer" of the Life Insurance Company Guarantee Corporation of New York.

For the year 1991, petitioner filed form CT-33, Franchise Tax Return for Insurance Corporations. On Schedule H of the return, Computation of Premiums, petitioner reported "Life insurance premiums" of \$5,011,469.00, "Accident and health insurance premiums" of \$9,998,633, and "Total" premiums of \$15,010,102.00.

For the same year petitioner filed a Federal Form 1120-PC, U.S. Property and Casualty Insurance Company Income Tax Return.

¹Petitioner was licensed in 1991 under the name of Financial Security Life Insurance Company, the name under which petitioner transacted business prior to 1992.

For the year 1992, petitioner filed form CT-33, Franchise Tax Return for Insurance Corporations. On Schedule H of the return, Computation of Premiums, petitioner reported "Life insurance premiums" of \$22,710,038.00, "Accident and health insurance premiums" of \$39,230,710.00, and "Total" premiums of \$61,940,748.00.

For the year 1992, petitioner filed an amended form CT-33, Franchise Tax Return for Insurance Corporations. On Schedule H of the return, Computation of Premiums, petitioner reported "Life insurance premiums" of \$22,710,038.00, "Accident and health insurance premiums" of \$39,230,710.00, and "Total" premiums of \$61,940,748.00.

For the same year petitioner filed a Federal Form 1120-PC, U.S. Property and Casualty Insurance Company Income Tax Return.

On May 31, 1994 and October 7, 1994, the Division issued to petitioner statements of proposed audit changes for tax due under Article 33 of the Tax Law for the years 1991 and 1992, respectively. In an attachment to the statements the Division informed petitioner that its tax on premiums had been recomputed and further explained that:

Section 801(a) of the Internal Revenue Code defines a life insurance company as an insurance company whose life insurance reserves plus unearned premiums and unpaid losses on life products comprise more than 50% of its total reserves. Since you did not meet the test of reserves to be treated as a life company, and are treated as a property and casualty company for Federal purposes, you are treated as a p & c company under Article 33. Only a life company may tax premiums at .8%.

The conclusion explains that rates for non-life companies are 1% for accident and health premiums and 1.2% (for 1991) or 1.3% (for 1992) for all other premiums.

In June of 1994, petitioner responded to the May 31, 1994 Statement of Proposed Audit Changes. The Division responded with a letter dated July 8, 1994, which stated:

the starting point for entire net income is either Federal taxable income or LICTI. The NYS Tax Law recognizes the difference in Federal taxation of life and non-life companies. The Audit Division requires Federal conformity and disagrees with the idea that the taxes imposed under Sections 1501 and 1510 are so separate and diverse that a company can be treated as a life company under one section and a non-life company under the other.

In addition, there have been precedent setting decisions in which it has been ruled that the purpose for which a company has been formed is irrelevant in determining the treatment for tax purposes. "It has been firmly established that classification for franchise tax purposes is to be determined by the nature of the corporation's business and that the purposes for which the corporation was organized are immaterial" (citation omitted).

On August 1, 1994 the Division issued a Notice of Deficiency (#L-008865671)² to petitioner in the amount of \$48,016.00 in tax, exclusive of interest. No penalties were asserted. The notice was for franchise tax on insurance corporations for the year 1991.

On November 17, 1994 the Division issued a Notice of Deficiency (#L-009591358) to petitioner in the amount of \$819,903.00 in tax, exclusive of interest. No penalties were asserted. The notice was for franchise tax on insurance corporations for the year 1992.

Petitioner requested a conciliation conference on each of these notices. On September 29, 1995 a combined Conciliation Order was issued setting forth the following recomputation of the statutory notices: #L-008865671 (1991) remained the same at \$48,016.00 in tax due, exclusive

²The Division did not introduce a copy of the Notice of Deficiency. Rather, it introduced a microfiche copy of the notice and an affidavit of a Division employee explaining the Division's practices and procedures regarding the retaining of microfiche copies rather than hard copies of notices. The evidence submitted is sufficient to establish that a notice was issued, especially since no question has been raised in these proceedings as to whether a notice was issued (*see, Matter of Huang*, Tax Appeals Tribunal, April 27, 1997.)

of interest; and #L-009591358 (1992) was recomputed from \$819,903.00 in tax due to \$258,660.00 in tax due, exclusive of interest.³

On December 19, 1995 the Division of Tax Appeals received the petition in this matter contesting both notices as recomputed by the Conciliation Order.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge concluded that the resolution of the controversy in this case was a matter of statutory construction. Relying on principles of statutory construction, she found that the present case involves the imposition of a tax, not the requesting of an exclusion or an exemption from tax. Therefore, petitioner is not required to prove that its interpretation of the statute is the only reasonable one or that the Division's interpretation is unreasonable.

The Administrative Law Judge noted that the Court of Appeals, in ***Guardian Life Ins. Co. of Am. v. Chapman*** (302 NY 226), held that provisions of the Tax Law which deal with the taxation of insurance companies and provisions of the Insurance Law dealing with the same general subject matter are *in pari materia* and "must be read together and applied harmoniously and consistently" (***Guardian Life Ins. Co. of Am. v. Chapman, supra***, at 231).

The Administrative Law Judge noted that petitioner is licensed to conduct the business of life insurance under the Insurance Law. Noting the statutory definition of a life insurance company under the Insurance Law, the Administrative Law Judge concluded that petitioner was a life insurance company for purposes of the Insurance Law and a life insurance corporation for purposes of Tax Law § 1510(b). The Administrative Law Judge also concluded that the term

³The recomputation concerned petitioner's utilization of net operating losses in 1992 which is not an issue in the current matter.

“transacting business” is not defined in the Tax Law but such term is not susceptible to being quantified pursuant to the provisions of Tax Law § 1510. Thus, based on the record, petitioner transacted the business of life insurance in New York State during the years at issue and was entitled to be taxed on its premiums at the lower rate provided in Tax Law § 1510(b).

The Administrative Law Judge rejected the Division's argument that, based on the holding in *McAllister Bros. v. Bates* (272 App Div 511, 72 NYS2d 532, *lv denied* 272 App Div 979, 73 NYS2d 485), petitioner was to be classified for franchise tax purposes by the nature of its business rather than the purposes for which it was organized. The Administrative Law Judge found that the rules generally applicable to construing franchise tax statutes under Articles 9 or 9-A are not necessarily applicable to an insurance company licensed to do a specific kind of business under the Insurance Law. Rather, the Administrative Law Judge concluded that the business activities of insurance corporations are more restricted than those of general business corporations.

Further, the Administrative Law Judge rejected the Division's argument that since petitioner files Federal income tax returns as a property and casualty insurance corporation for Federal purposes, it cannot be a life insurance corporation under Tax Law § 1510. The Administrative Law Judge concluded that Tax Law Article 33 does not require conformity with the Internal Revenue Code's definition of life insurance company nor does a definition of a life insurance company in terms of its corporate reserves (as provided pursuant to Internal Revenue Code § 816) have any relation to a franchise tax based on premiums received.

ARGUMENTS ON EXCEPTION

On exception, the Division agrees with the facts found by the Administrative Law Judge and requests an additional finding of fact indicating that on its Form CT-33 for 1992, petitioner made property and casualty company addition and subtraction modifications in computing its entire net income. The Division argues that the Administrative Law Judge erred in her conclusion that petitioner is a life insurance corporation for purposes of Tax Law § 1510 and erred in concluding that the Federal income classification of petitioner was irrelevant to Article 33. Further, the Division alleges that the Administrative Law Judge erred in her reliance on the Insurance Law in order to classify petitioner as a life insurance company for purposes of Tax Law § 1510. The Division contends that petitioner was required to compute its Tax Law § 1510 additional tax on premiums as a non-life insurance company.

The Division argues that since petitioner is challenging the interpretation of a statute by the agency which administers it, petitioner bears the burden of proving that the Division's interpretation is irrational or unreasonable and that petitioner's interpretation is the only logical interpretation. Pursuant to Internal Revenue Code § 816, petitioner filed its Federal income tax returns as a property and casualty insurance company for the years in issue. In the Division's view, this fact alone precludes petitioner from claiming that it is a life insurance corporation under Tax Law § 1510. The Division asserts that petitioner cannot be one type of insurance company for purposes of calculating its entire net income pursuant to Tax Law § 1503 and another type of company for purposes of the Tax Law § 1510 additional tax on premiums. The Division argues that Tax Law § 1503, in referring to Federal "life insurance taxable income" and Federal "taxable income," distinguishes between life insurance corporations and non-life

insurance corporations. Thus, the Division claims that, petitioner, having calculated its entire net income pursuant to Tax Law § 1503 as a non-life insurance corporation, cannot calculate the Tax Law § 1510 additional tax on premiums as a life insurance company.

The Division argues that the reliance by the Administrative Law Judge and petitioner on petitioner's authorization under the Insurance Law to conduct a life insurance business in New York State rather than on petitioner's classification for Federal income tax purposes was misplaced. To hold otherwise, states the Division, would be to allow an insurance company authorized to sell life insurance to conduct only a minimal amount of life insurance business in order to obtain the lower Tax Law § 1510(b) tax rate on premiums. This, alleges the Division, is contrary to the legislative intent in enacting Article 33.

The Division points out that prior to the enactment of Article 33 in 1974, insurance companies were subject to a premium tax imposed by Tax Law former § 187. Under Article 33, both life and non-life insurance companies were subjected to tax both on entire net income and on premiums. The Division argues that legislative changes made in 1987 were made to ameliorate the effects of the 1986 Federal Tax Reform Act on the New York insurance industry and that this legislation envisioned that a company's classification for Tax Law § 1501 purposes would be the same as for Tax Law § 1510 purposes. The Division states that the Administrative Law Judge incorrectly relied on *Guardian Life Ins. Co. of Am. v. Chapman (supra)* as requiring conformity of Tax Law § 1510 with the Insurance Law. Rather, the Division urges that the legislative history surrounding the enactment and amendments to Article 33 should control.

Petitioner argues, in opposition, that the Administrative Law Judge correctly concluded that a determination of whether petitioner is a "life insurance corporation" for purposes of Tax

Law § 1510 is a matter of statutory construction and that the plain language of the statute makes clear that petitioner is subject to tax at the rates specified in Tax Law § 1510(b). Petitioner contends that because the language of Tax Law § 1510 clearly supports its position, it is unnecessary to look beyond the statute to legislative history in order to discern the meaning of the enactment. Further, petitioner asserts that its interpretation is the only logical interpretation of Tax Law § 1510. However, petitioner states that if resort to legislative history is necessary, it supports petitioner's position rather than that advanced by the Division.

Petitioner contends that there is no express statutory language or any indication of an intent that the Legislature, in enacting Article 33 and imposing a franchise tax on insurance companies measured by entire net income or capital, changed the recognized meaning of "life insurance corporation" as that term was used in the premiums tax to "life insurance company" as that term is used in the Internal Revenue Code. In fact, the premiums tax was carried through the 1973 and 1974 legislation without substantive legislative change and with legislative documents that provide that no substantive change was made or contemplated.

Petitioner argues that since Tax Law § 1510 levies a tax and does not provide for a deduction, credit or exclusion, it must be narrowly construed and any doubts as to its application must be resolved in petitioner's favor. Thus, alleges petitioner, the Division and not petitioner must show that its interpretation of Tax Law § 1510 is the only correct interpretation. Petitioner states that the plain meaning of Tax Law § 1510 is clear -- it distinguishes between a) life insurance corporations that are authorized to do business in New York and b) insurance corporations except life insurance corporations that are authorized in New York, but do not transact the business of life insurance. While the term "life insurance corporation" is not

specifically defined in the Tax Law, petitioner argues that the Tax Law has defined insurance companies by reference to the laws of New York under which the company is organized and authorized to do an insurance business both before and after the enactment of Article 33. Thus, petitioner contends that it is the Insurance Law and not Federal income tax law which defines the term "life insurance corporation." As petitioner is a life insurance corporation which transacted the business of life insurance in the years at issue, it argues that it is properly taxed under Tax Law § 1510(b) and not Tax Law § 1510(a). Petitioner asserts that the Administrative Law Judge correctly relied on the decision of the Court of Appeals in *Guardian Life Ins. Co. of Am. v. Chapman (supra)* and found that Tax Law § 1510 is *in pari materia* with the Insurance Law.

Petitioner states that the Division's position that petitioner's status as a "life insurance company" or "insurance company other than life" for Federal tax purposes governs its status for purposes of the franchise tax imposed on income pursuant to Tax Law § 1501 and the tax on premiums imposed pursuant to Tax Law § 1510 is without merit. Petitioner states that this position is also contrary to the decision of this Tribunal in *Matter of United States Life Ins. Co.* (Tax Appeals Tribunal, April 2, 1992) in which we stated: "[t]he Federal income tax imposed on insurance corporations by the Internal Revenue Code is separate and distinct from the franchise tax imposed by Tax Law § 1501."

OPINION

In addition to the franchise tax imposed by Tax Law § 1501(a) on every domestic, foreign and alien insurance corporation for the privilege of exercising its corporate franchise or doing business or employing capital or owning or leasing property in New York, Tax Law § 1510 imposes a tax on premiums on risks located or resident in New York.

Tax Law § 1510(a) provides:

every . . . insurance corporation . . . authorized to transact business in this state under a certificate of authority from the superintendent of insurance *other than such corporations transacting the business of life insurance*, shall, for the privilege of exercising corporate franchises . . . pay a tax on all gross direct premiums, less return premiums thereon, written on risks located or resident in this state (emphasis added).

Tax Law § 1510(b) provides:

every . . . life insurance corporation . . . authorized to transact business in this state under a certificate of authority from the superintendent of insurance, shall . . . pay a tax on all gross direct premiums, less return premiums thereon, received in cash or otherwise on risks resident in this state

The matter for resolution herein is under which section petitioner must calculate the additional tax on its premiums for the years at issue. Necessarily, this decision turns on whether petitioner is a life insurance corporation or an insurance corporation other than a life insurance corporation.

On exception, the Division raises several of the same arguments that it presented to the Administrative Law Judge. However, it also argues that the legislative history surrounding Article 33 of the Tax Law provides significant support for its position. Specifically, the Division argues that the changes to Article 33 enacted pursuant to Chapter 817 of the Laws of 1987 "makes it clear that the legislature intended that a life company for § 1501 purposes is a life company for premiums tax purposes and a non-life company for § 1501 purposes is a non-life company for premiums tax purposes" (Division's reply brief, p. 16). The Division defines a "life company for § 1501 purposes" by reference to Internal Revenue Code § 816. That section, in turn, defines a life insurance company as one which is engaged in the business of issuing life

insurance and annuity contracts if its life insurance reserves plus unearned premiums and unpaid losses not included in life insurance reserves comprise more than 50% of its total reserves.

We disagree with the Division's analysis. The legislative history cited by the Division contains only the most cursory explanation for the numerous sections of Chapter 817 that amended Article 33 of the Tax Law. A review of each of those amendments gives no indication that the Legislature intended that the provisions of the Internal Revenue Code prescribing the manner in which insurance companies are to report their income for Federal income taxation purposes are deemed to be controlling to determine whether an insurance corporation is a life or non-life corporation for purposes of Article 33.

On reviewing the record before the Administrative Law Judge, we find that the Administrative Law Judge thoroughly considered the issues before her and correctly applied the applicable law in arriving at her conclusions. We agree with the Administrative Law Judge that the plain language of the relevant statutes makes clear that petitioner is not subject to tax pursuant to Tax Law § 1510(a) but pursuant to Tax Law § 1510(b). We also agree with her conclusion that the provisions of Article 33 of the Tax Law which deal with the taxation of insurance companies and the provisions of the Insurance Law dealing with the same general subject matter are to be read *in pari materia*. As did the Administrative Law Judge, we find no support for the Division's argument that the classification of an insurance corporation for purposes of Tax Law § 1510 for franchise tax purposes is controlled by the provisions of the Internal Revenue Code applicable to the taxation of income of insurance corporations. Thus, we agree with the Administrative Law Judge that petitioner has demonstrated that it was a "life insurance company" under Insurance Law § 107(a)(28) (i.e., a corporation having power to do

either the business of life insurance or annuities or both) and that petitioner was correct in calculating its additional franchise tax on premiums pursuant to Tax Law § 1510(b) rather than pursuant to Tax Law § 1510(a). As a result, we affirm the determination of the Administrative Law Judge for the reasons set forth therein.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is denied;
2. The determination of the Administrative Law Judge is sustained;
3. The petition of First Fortis Life Insurance Company is granted; and
4. The notices of deficiency dated August 1, 1994 (#L-008865671) and November 17, 1994 (#L-009591358) are cancelled.

DATED: Troy, New York
June 11, 1998

/s/Donald C. DeWitt

Donald C. DeWitt
President

/s/Carroll R. Jenkins

Carroll R. Jenkins
Commissioner

/s/Joseph W. Pinto, Jr.

Joseph W. Pinto, Jr.
Commissioner