

## Proposed New York State Tax Changes Contained in Governor's 2015-16 Budget

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### Overview

On January 21, 2015, New York State Governor Andrew Cuomo presented the 2015-2016 New York State Executive Budget, which includes proposed technical corrections to the New York State tax reform provisions enacted in 2014,<sup>1</sup> changes to the sales tax, and other proposals. The 2015-2016 Budget also includes broad-based reform of the New York City corporate tax regime, the proposed provisions of which are generally consistent with the New York State tax reform provisions enacted in 2014. In this Tax Alert we summarize the more significant New York State tax reform proposals included in the Executive Budget.<sup>2</sup>

### Proposed Technical Corrections and Other Revisions to the 2014 New York State Tax Reform

The more significant proposed technical corrections and other revisions to the New York State Tax Reform provisions enacted in 2014 include the following:

- Clarifying that, in order to qualify as investment capital, stock must never have been used by the taxpayer in the regular course of the taxpayer's business
- Clarifying that the presumption that stock acquired in the second half of the taxable year would satisfy the required holding period to be considered investment capital would not apply if the taxpayer in fact does not own the stock when it files its original tax return for the taxable year in which it acquires the stock
- Removing the subtraction of hedging losses and expenses from the computation of nontaxable investment income, (the original provision essentially would have disallowed those expenses)
- Clarifying that, for purposes of computing the residential and small business loan subtraction modification for certain community banks and small thrifts, the \$8 billion asset qualifying test for a combined group applies if the taxpayer is included in a combined report and the assets of the combined group do not exceed \$8 billion and clarifying generally that the modifications for certain community banks and small thrifts do not reduce the numerator and denominator of the apportionment fraction
- Clarifying that only unitary group members are considered in applying the aggregate bright-line economic nexus tests; in other words, only the New York receipts of \$10,000 or more of unitary group members would be aggregated to determine whether the \$1 million or more bright-line nexus threshold is met
- Clarifying that, for purposes of qualifying as a "qualified New York manufacturer" (for a 0% tax rate on the business income base), a combined group filing a combined report would be required to meet the "principally engaged" test on a combined basis
- Limiting the type of New York property required in order to qualify as a qualified New York manufacturer (under one of the two statutory tests) to New York ITC property that is "principally used by the taxpayer in the production of goods by manufacturing, processing, assembling, refining, mining, extracting, farming, agriculture, horticulture, floriculture, viticulture or commercial fishing," whereas the New York property requirement previously had been satisfied with any New York ITC property (such as research and development property)
- Clarifying that each corporation in a combined group must qualify as a qualified emerging technology company ("QETC") for the reduced QETC rates to apply
- Providing that the investment tax credit applicable to certain financial institutions may not be taken for property first placed in service on or after October 1, 2015, and restoring to the statute providing such credit, language permitting the aggregation of use by certain affiliates to meet the statutory use requirement

<sup>1</sup> Our April 1, 2014, Tax Alert summarizing the 2014 New York State law changes is available [here](#).

<sup>2</sup> In this Tax Alert we do not address the related New York City corporate tax reform proposals. Our January 23, 2015, Tax Alert summarizing the New York City proposals is available [here](#).

- Establishing a capital base rate of 0.132% for tax years beginning in 2015 for qualified New York manufacturers and QETCs and adding new fixed dollar minimum tables for S corporations that are manufacturers or QETCs
- Clarifying that the deduction related to pre-2015 net operating losses (the Prior Net Operating Loss Conversion “PNOLC” subtraction) can be claimed only until the calculated pool of pre-2015 net operating losses is exhausted, and, except where the taxpayer elects to use its entire pool of pre-2015 net operating losses in 2015 and 2016 (as elected on its first return for the 2015 tax year), the taxpayer may carry forward the PNOLC subtraction pool for no longer than 20 taxable years or until the 2035 tax year, whichever comes first
  - Clarifying that an NOL must be carried back to the earliest year first; and providing that a taxpayer may make an irrevocable election on an original return (a separate election for each loss year) to waive the entire carryback period
- Amending the apportionment provisions:
  - Broadening the definition of “qualified financial instrument” by including those financial instruments *eligible or required to be* marked to market under I.R.C. §§ 475 or 1256 (as opposed to those actually marked to market by the taxpayer);
  - Deleting “the location of the treasury function of the business entity” as the first level in the hierarchy for purposes of determining commercial domicile in sourcing receipts from financial transactions;
  - Adding apportionment provisions for marked-to-market net gains, receipts from the operation of vessels and qualified air freight forwarders; and
  - Clarifying that a loan is “secured by real property” if 50% or more of the collateral used to secure the loan (based on fair market value at the inception of the loan) consists of real property
- Eliminating the requirement that the designated agent of a combined group, which acts on behalf of the members of the group relating to the combined report, must be the parent corporation

These proposals would be effective as if originally enacted as part of the 2014 Tax Reform, which generally would be for tax years beginning on or after January 1, 2015. Based on this effective date language, however, the amendments to the provisions determining the qualifications of a qualified New York manufacturer (for purposes of the zero tax rate on business income) may be retroactive to taxable years beginning on or after January 1, 2014.

### Changes to the Sales Tax

- Amending the tax law by adding a new section 1118-A, Limitations on “tax avoidance strategies,” as broadly worded in the proposed Executive Budget:
  - Requiring that a nonresident entity be liable for New York use tax on item(s) purchased outside of New York (when the entity was a nonresident of New York) and subsequently brought into New York unless the out-of-state entity was doing business outside of New York for at least six months prior to bringing the property into New York
  - Deeming a single member limited liability company (“LLC”) and the LLC’s member to be one person so that the purchase or sale by either the LLC or its single member will be deemed a purchase or sale by the other; therefore, neither the LLC nor the single member will be able to purchase an item for resale from the other
  - Requiring sales tax to be imposed at the inception of a lease between related parties on all payments required under the lease
  - Expanding the provision under New York Tax Law § 1111(q) in order to eliminate any tax-free transfers of tangible personal property between affiliated corporations or partnerships in exchange for stock of the corporation or for an interest in the partnership, or in the case of distributions of property back to a stockholder or partner upon liquidation (note that under current New York Tax Law § 1111(q), only tax-free transfers, contributions or distributions of aircraft and vessels between affiliated corporations or partnerships in exchange for the stock or interest in the corporation or partnership or a distribution of property back to a stockholder or partner are precluded from tax-free treatment)
    - The only exception would be where property is transferred to a corporation in exchange for stock under a merger plan, and New York would allow a credit against sales or use tax due as the result of a transfer, contribution or distribution for sales or use tax previously paid to New York or another state on the purchase or use of the transferred property

- If passed, it appears that contributions to capital and distributions of property would become subject to New York sales tax
  - This proposal would take effect immediately and apply in accordance with applicable transitional provisions of §§ 1106 and 1217 of the New York Tax Law
- Requiring marketplace providers to collect sales tax on taxable sales that they facilitate
  - Defining “marketplace provider” to mean a person who collects the purchase price, as well as performs one of the other specified sales functions such as providing the physical or virtual forum where the transaction takes place
  - Requiring a marketplace provider to perform all duties of a vendor, including the collection of sales tax, filing of sales and use tax returns and the remittance of sales tax
  - Requiring only marketplace providers that have sufficient presence in New York to collect the tax
    - This proposal would take effect March 1, 2016, and would apply in accordance with the transition provisions in §§ 1106 and 1217 of the New York Tax Law
- Expanding the sales and use tax exemption for residential and commercial solar equipment to include electricity that is purchased from a seller primarily engaged in the sale of solar energy systems equipment and/or electricity generated by such equipment if the electricity is sold under a written agreement and is generated by equipment that is: (1) owned by a person other than the purchaser of the electricity; (2) installed at the purchaser’s residence or non-residential premises; and (3) used to provide heating, cooling, hot water or electricity
  - This proposal additionally amends existing local option provisions to include the expanded exemption and would take effect on December 1, 2015
- Adding “prepaid mobile calling services” to the definition of “prepaid telephone calling service” in order to clarify that retailers must apply the same rules they apply to prepaid telephone calling services in determining the incidence of the sales tax
  - The rule that the sale is sourced to the location of the retailer where the customer bought the service, whether the customer is initiating the account or recharging an existing account there, will generally apply
  - This proposal would take effect immediately
- Exempting from New York use tax beer, cider and liquor used at tastings held in conformity with the Alcoholic Beverage Control Law, as well as several types of items used to package such beverages
  - This proposal would take effect June 1, 2015, and would apply in accordance with the transition provisions in §§ 1106 and 1217 of the New York Tax Law
  - Clarifying that, in addition to wine and wine product, certain types of items used to package such wine or wine product furnished to customers for a wine tasting held in accordance with the Alcoholic Beverage Control Law are exempt from sales tax; this proposal would take effect immediately

### Other Proposed Changes

- Amending the investment tax credit by limiting the investment credit base of a master of a film, television show or commercial solely to those costs associated with the creation, production or reproduction of such film, television show or commercial that were incurred within New York State and excluding from the base those costs used by the taxpayer (or any other taxpayer) in the calculation of any other credit allowed under the New York Tax Law
  - Amending the qualified New York manufacturer provisions to specifically exclude the license of a master of a film, television show or commercial as “the sale of a good” for purposes of meeting the “principally engaged” test, a prerequisite to qualifying as a qualified New York manufacturer, requiring that more than 50% of the gross receipts of the taxpayer (or combined group) must be derived from the receipts from the sale of goods produced by manufacturing-type activities
  - These provisions would be effective for taxable years beginning on or after January 1, 2016
- Amending the Excelsior Jobs Program (“EJP”) tax credit to include a new category of qualifying businesses eligible for the program called “entertainment companies”
  - This is defined to include a wide range of companies, including film production, radio production, and video game production, among others
- Reforming the New York Industrial Development Agency (“IDA”) program to expand recapture/claw-back provisions and reporting requirements of IDAs

- Requiring IDAs to maintain certain information on their web sites, including copies of resolutions, names of officers, public notice of all meetings at least 10 days in advance, meeting agendas and minutes; requiring approval from Department of Economic Development before providing exemptions from state taxes
- Modifying the Brownfield Clean-up Program: excluding from eligibility amounts paid to related parties, limiting participation to projects that are accepted into the Brownfield Clean-up program by December 31, 2022, and requiring that certificates of completion be received by December 31, 2025
- Creating the Employee Training Incentive Program, which would convey refundable tax credits for qualified activities equal to 50% of eligible training costs, up to \$10,000
- Reducing the net income tax on small business taxpayers (generally defined as businesses having not more than \$390,000 of business income for the taxable year and less than 100 full time employees) from 6.5% to rates of 3.25% for 2016, 2.9% for 2017 and 2.5% for 2018 and thereafter for taxpayers with not more than \$290,000 of business income, with higher rates phasing in for taxpayers with business income over \$290,000 and not more than \$390,000
- Levying taxes under New York Tax Law §§ 184 and 184-a (the franchise tax on transportation and transmission corporations and the related Metropolitan Transportation surcharge), on wireless telecommunications businesses, for tax years beginning on or after January 1, 2015

### Considerations

To be considered “on time,” the 2015 Budget must be passed by March 31, 2015. If that timing is achieved, for financial statement purposes it would affect the interim reporting period that includes the enactment date. However, any of the proposals described above could be amended or entirely deleted prior to enactment.

### Contacts

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