New York Updates Guidance on Post-TCJA Interest Deduction Attribution

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By Paige Jones

Corporate taxpayers with repatriated income or limitations under IRC section 163(j) must take modified steps when using New York's method for attributing interest deductions, according to the state's tax agency.

A June 12 technical memorandum (TSB-M-19(2)C, (2)I) from the New York State Department of Taxation and Finance says that in light of recent federal tax code changes, general business corporate taxpayers are required to take certain steps when using the state tax agency's 2015 guidance on the attribution of interest deductions.

"A taxpayer or the designated agent of a combined group must modify the attribution methodology in the 2015 TSB-M when the federally deductible interest expense is limited by IRC section 163(j) in the current tax year *and* either: it has not made the 40 percent safe harbor election; *or* it has made the 40 percent safe harbor election and the taxpayer (or combined group) owns exempt cross-article stock," the memo says (emphasis in original).

The tax agency describes the four-step process for business corporate taxpayers, instructing readers to use the steps described in the 2015 guidance but with the 2019 memo's computed amounts.

"This new technical memo, which the tax department says must be read in conjunction with the 2015 memo, further complicates an already difficult area because of changes made to the business interest expense deduction rules under federal tax reform," Timothy Noonan of Hodgson Russ LLP told *Tax Notes* June 13.

Sebastian C. Watt of Reed Smith LLP cautioned taxpayers to "pay close attention" to the memo. "The TSB modifies the department's prior interest attribution rules, which may impact taxpayers' deductions for investment income, exempt [controlled foreign corporation] income, and exempt unitary corporation dividends," Watt told *Tax Notes.*

For combined groups, the memo "implies that a New York combined group tests the section 163(j) limitation on a combined-group basis," said Jennifer White, also of Reed Smith. "This is consistent with New York statute, which treats a combined group as a single taxpayer," she added in a June 13 email.

Regarding repatriated income, the memo says that if a foreign corporation's stock that generates the section 965(a) inclusion amount is investment capital, then the stock is included in the indirect attribution formula for investment capital. It is not considered exempt CFC stock, the memo adds. However, if a foreign corporation's stock that generates the IRC section 965

inclusion amount is business capital, that stock is considered exempt CFC stock and follows the 2015 guidance, the memo says.

Noonan lamented the department's delay in issuing this updated guidance, pointing out that it was issued 17 months after federal tax reform and after most taxpayers had filed their 2018 returns.

"It's another example of how states, practitioners, and taxpayers are going to be dealing with the fallout from federal tax reform for years to come," Noonan said.