



# Comptroller v. Wynne: Implications for New York State

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# COMPTROLLER OF THE TREASURY OF MARYLAND v. WYNNE

- 5-4 decision by U.S. Supreme Court decided on May 18, 2015
- MD imposed state and county-level taxes on all income of residents; allowed resident credit only against state tax
- Held: MD's personal income tax scheme violates the dormant Commerce Clause





# MARYLAND'S PERSONAL INCOME TAX ON RESIDENTS

- MD residents (like NY residents) pay tax on their worldwide income
- MD personal income tax has two components: (1) state and (2) county
- Nonresidents only pay tax on sourced income, but they pay BOTH the state and county tax (called “special nonresident tax”)
- Residents only allowed credit against state portion of tax

# FACTS IN WYNNE

- MD residents who held stock in an S corp that operated and filed returns in 39 other states
- Reported flow-through income from the S corp on MD income tax returns
- Claimed resident tax credit (against both the state and county components) for taxes paid to other states
- The MD State Comptroller disallowed credit against county component



# ON TO THE SUPREME COURT

During Oral argument, Chief Justice John Roberts observed that:

*“if each State did what we’re talking about, people who work in one State and live in another would pay higher taxes overall than people who live within one State and work in the same State.”*



# THE INTERNAL CONSISTENCY TEST

- Justice Roberts was talking about the “Internal Consistency Test”: the Commerce Clause requires that taxes on interstate commerce be nondiscriminatory and fairly apportioned.
- This test is designed to allow us to distinguish between: (i) a tax structure that is inherently discriminatory (bad); and (ii) one that might result in double taxes only as a result of two nondiscriminatory state schemes (OK)
- Past cases may have suggested that the Commerce Clause was n/a to individual income taxes; the Court laid that to waste.

# THE INTERNAL CONSISTENCY TEST

*The test: whether interstate and intrastate commerce would be taxed equally if every state were to adopt the precise tax scheme at issue*

- State A imposes a 1.25% tax on all residents, regardless of where earned.
- State A also imposes a tax on nonresidents' source income at 1.25%
- No resident credits
- April and Bob live next door to each other in State A; Bob's business located in State B; April's is all in State A.
- To apply the I/C test, we have to assume all states have the State A scheme. State A fails the test!!

	April	Bob
State A Tax	1.25%	1.25%
Hypo State B Tax	0	1.25%
Total Bill	1.25%	2.5%

# THE INTERNAL CONSISTENCY TEST: PASSING GRADE?

Could this be *cured* in order to pass the Internal Consistency Test?

- State A imposes a 1.25% tax on all residents, regardless of where earned.
- State A also imposes a tax on nonresidents' source income at 1.25%
- *State A provides resident credit for taxes paid to other states on sourced income*
- April and Bob live next door to each other in State A; Bob's business located in State B; April's is all in State A.

	April	Bob
State A Tax	1.25%	0
Hypo State B Tax	0	1.25%
Total Bill	1.25%	1.25%



# THE INTERNAL CONSISTENCY TEST: PASSING GRADE?

*Could this be cured in order to pass the Internal Consistency Test?*

- State A imposes a 1.25% tax on all residents, regardless of where earned.
- *State A does not tax on nonresidents*
- No resident credits
- April and Bob live next door to each other in State A; Bob's business located in State B; April's is all in State A.

	April	Bob
State A Tax	1.25%	1.25%
Hypo State B Tax	0	0
Total Bill	1.25%	1.25%

- But is this fairly apportioned – externally consistent?

# THE INTERNAL CONSISTENCY TEST: BE CAREFUL

*Don't get lost in the differences between the rules in two states*

- State A imposes a 1.25% tax on all residents, regardless of where earned.
- *State A does not tax on nonresidents and provides no resident credits (which is internally consistent per previous slide)*
- But assume State B is a *real state*; and it *does tax* nonresidents
- April and Bob live next door to each other in State A; Bob's business located in State B; April's is all in State A.

	April	Bob
State A Tax	1.25%	1.25%
<i>Actual</i> State B Tax	0	1.25%
Total Bill	1.25%	2.5%

- This stinks for Bob. And there is double tax. But NOT because State A's scheme fails the test; only because of what State B is doing.

# THE AFTERMATH OF WYNNE

- Commerce Clause protections extend equally to:
  - Taxes based on gross and net income (prior cases generally focused on gross receipts taxes); and
  - Both corporations and individuals (prior cases generally dealt with corporations)
- Maryland counties to pay more than \$200 million in refunds
- Consider filing refund claims—in MD, and maybe even elsewhere?

# QUESTIONS REMAIN

- *Must NYS allow resident credit against NYC personal income taxes for source income in other states?*
- CA is typical example, since NYC resident with source income pays 13% to CA and only gets credit against 8% NYS tax.
  - No longer can say Commerce Clause n/a to individuals
  - Unlike MD, NYC doesn't tax nonresidents
  - But see slide 9: fair apportionment?





# QUESTIONS REMAIN

- *Is NY's Statutory Residency Test unconstitutional?*
- Court of Appeals in *Tamagni* upheld rule; declined to apply Commerce Clause analysis, but said that rule was fine anyway even if it did
  - How does the *Wynne* rule, that the Commerce Clause applies to individuals, affect the analysis?
  - Must a credit be provided for taxes paid to other states in all circumstances?
  - Different rule for “non-sourced” income?
  - 1995 NESTOA agreement attempted to remedy (see attached article)



# QUESTIONS REMAIN

- *Is NY's convenience rule unconstitutional?*
- Court of Appeals in *Zelinsky* upheld rule; applied Commerce Clause analysis and said that rule was fine
  - No question about IC test; taxpayer conceded the rule passed.
  - External consistency was issue
  - But what about reverse-convenience days?



# QUESTIONS?



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