HODGSON RUSS LLP'S REPORT ON THE 2017-18 NEW YORK STATE BUDGET

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On April 10th, the New York State budget for 2017-18 was signed into law. The highlights of the revenue provisions are summarized below.

Personal Income Tax

- **"Millionaires Tax" Extended.** The top tax bracket (rate of 8.82%) is extended for two years (for taxable years 2018 and 2019). It was previously scheduled to expire for taxable years beginning after 2017.
- **Limit Extended on Charitable Contribution Deductions.** The NYS itemized charitable tax deduction limits in Tax Law § 615(g)—50% of the federal deduction for individuals with NYAGI between $1 million and $10 million and 25% of the federal deduction for individuals with NYAGI over $10 million—was set to expire at the end of 2017, at which point all taxpayers with NYAGI over $1 million would have been subject to a 50% limitation. However, the 25% limitation for individuals with AGI over $10 million has been extended through the end of 2019. Conforming amendments are also made to NYC Administrative Code § 11-1715(g).
- **Sales of Partnership Interests by Nonresidents May be Taxable.** Under prior law, the sale of a partnership interest by a nonresident would normally not give rise to New York source gain or loss (the exception being if the partnership interest itself was used in a trade or business carried on in New York). Under the new law, if IRC § 1060 is in effect because, for example, the partnership has an IRC § 754 election in place, the gain recognized by the nonresident partner will be treated as New York source income "allocated in a manner consistent with the applicable methods and rules for allocation under this article . . . ." It is not clear how this new provision will be administered, but presumably it is designed to avoid the "free basis step-up" to a partnership's assets that would have occurred under prior law when a nonresident sold an interest in the partnership and it had an IRC § 754 election in effect. This provision is effective "immediately", and presumably applies to partnership interest sales occurring on and after April 10, 2017.
- **Disregarded Entities Treated as Single Taxpayer.** Under new Tax Law § 43, a single member LLC ("SMLLC") that is disregarded for federal income tax

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purposes must also be disregarded for purposes of determining whether the taxpayer that includes the SMLLC satisfies the requirements to be eligible for tax credits against, *inter alia*, the personal income tax and franchise tax. Tax Law § 43 also requires that if the taxpayer is the sole member of multiple LLCs, the sole member and all LLCs are treated as a single entity. This new provision is effective immediately and applies to "all taxable years for which the statute of limitations for seeking a refund or assessing additional tax is still open."

Sales and Use Taxes

- **Deferral Technique for Related Entities Eliminated.** The new legislation thwarts the ability of related entities to purchase tangible personal property ("TPP") or services exempt from sales tax under the resale exemption thereby deferring the sales tax. The legislation amends the definition of "retail sale" to include any transfer of TPP to certain entities when the property would be resold to related persons or entities, including; (1) sales to single member LLCs or subsidiaries that are disregarded for federal income tax purposes, for resale to a member or owner; (2) sales to a partnership for resale to one or more partners; and (3) sales to a trustee for resale to a trust beneficiary. This provision is effective immediately.
- **Energy Transportation, Transmission and Distribution Services.** Tax Law § 1105-C is amended to clarify that sales tax applies to charges for the transportation, transmission, or distribution of natural gas and electricity when such transportation, transmission, or distribution is provided by the provider of the commodity, *except* in those areas of the state in which the PSC has approved a "single retailer model." This provision is effective immediately.

Business-Related Taxes

- **Investment Tax Credit Reform.** The Investment Tax Credit ("ITC") statutes (Tax Law §§ 210-B and 606) are amended by identifying certain uses of property for which the ITC is not allowed. Under the amendments, the ITC cannot be claimed for property used by the taxpayer "in the production and distribution of electricity, natural gas after extraction from wells, steam, or water delivered through pipes and mains." These amendments take effect immediately.
- **Qualified Financial Instruments for RICs and REITs.** The new law excludes from the definition of "qualified financial instrument" mortgages, instruments that are "investment capital", and instruments that produce "other exempt income" if such instruments are held by stand-alone (i.e. not captive) RICs and REITs. This provision is effective for tax years beginning after 2015.

Other Tax Credits

- **Film Credits.** The Empire State Film Production Tax Credit and Empire State Film Post-Production Tax Credit is extended for three years through 2022.
- **Life Science Credits.** The benefits of the Excelsior Jobs Program Act are now extended to qualified life sciences companies. In addition, a new refundable credit is established for life science businesses qualifying as a "new businesses." The credit amount is generally 15% of the "research and development expenditures" under by IRC § 41(b) (20% for small businesses) and is capped at $500,000 per taxpayer and $10 million in the aggregate per year. These amendments will apply to taxable years beginning on or after January 1, 2018.

- **Alternative Fuels Property and Electric Vehicle Recharging Property Credit.** The Alternative Fuels and Electric Vehicle Recharging Property Credit is extended for five years, through tax years beginning in 2022.

Collections and Enforcement Provisions

- **Warrantless Bank Account Data Matching.** The bill expands the State's financial institution data matching program for state tax collection purposes to include information regarding financial accounts for tax debtors with fixed and final tax debts, whether or not a warrant has been filed. This provision is effectively immediately, and will expire on April 1, 2020.

- **Warrantless Wage Garnishment Extended.** The 2013 legislation authorizing warrantless wage garnishments, which was due to expire on April 1, 2017, was extended through April 1, 2020.

Please contact a member of our State and Local Tax practice group if you have any questions about this budget.