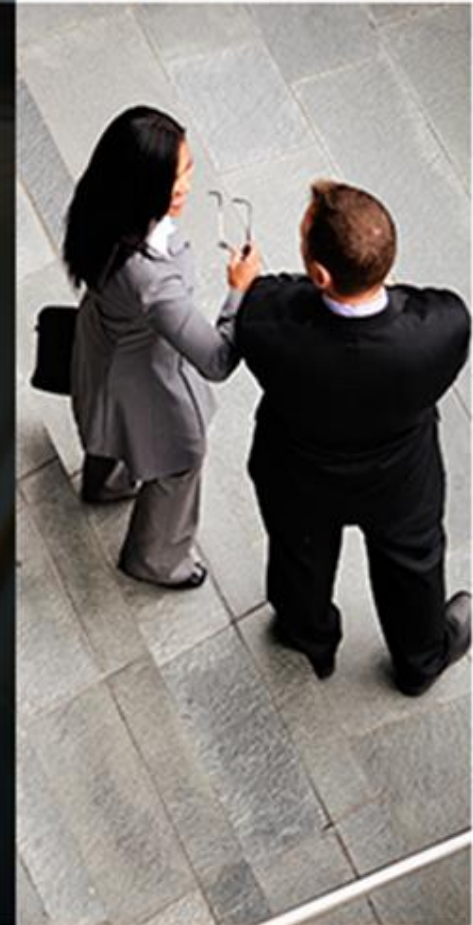


New York Tax Update

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TOPICS

- 2017-2018 Budget Bill
- Income Tax Hot Topics and New Cases
- Sales Tax Hot Topics and New Cases
- Corporate Tax Hot Topics and New Cases
- Compliance/Enforcement Hot Topics and New Cases

TOPICS

2017-2018 Budget Bill

BUDGET: “MILLIONAIRES TAX” EXTENDED

- Top tax rate (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



BUDGET: LIMIT EXTENDED ON CHARITABLE CONTRIBUTION DEDUCTIONS

- Current NYS itemized charitable tax deduction limits :
 - NYAGI \$1-10 million: 50% of federal deduction
 - NYAGI over \$10 million: 25% of federal deduction
- Current limits were set to expire after 2017, at which point all taxpayers with NYAGI over \$1 million would have been subject to a 50% limitation
- But the 25% limitation (for AGI > \$10M) was extended through the end of 2019
- Conforming amendments to NYC Admin. Code § 11-1715(g)

BUDGET: SALES OF PARTNERSHIP INTERESTS BY NONRESIDENTS MAY BE TAXABLE

- **Prior Law:** Generally no NY-source income on sale of partnership interest by nonresident (unless used in NY trade/business)
- **New Law:** If IRC § 1060 is in effect 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”
 - *E.g.*, partnership has an IRC § 754 election in place
 - Unclear how new rule 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
 - Effective “immediately”, and presumably applies to partnership interest sales occurring on and after April 10, 2017

BUDGET: DISREGARDED ENTITIES TREATED AS SINGLE TAXPAYER

- New Tax Law § 43 enacted
- SMLLC that is disregarded for federal income tax 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
- If taxpayer is the sole member of multiple LLCs, the sole member and all LLCs are treated as a single entity
- 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”

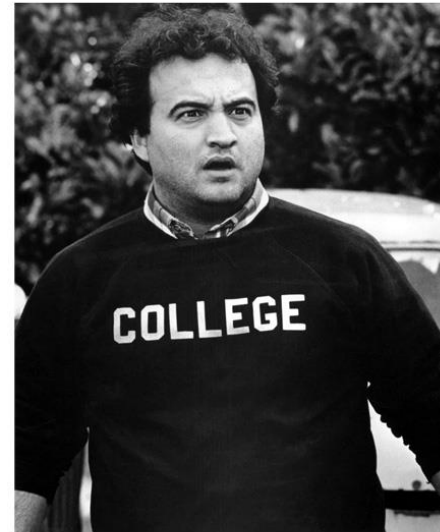
BUDGET: DEFERRAL TECHNIQUE FOR RELATED ENTITIES ELIMINATED

- Definition of “retail sale” amended
- Prevents related entities from purchasing TPP or services exempt from sales tax under the resale exemption
- “Retail sale” now includes any transfer of TPP to certain entities when the property would be resold to related persons or entities, including:
 1. Sales to SMLLCs or subs 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
- Effective immediately



FREE TUITION IN NYS FOR THE “MIDDLE CLASS”

- Income-qualifying students attend college tuition-free at all CUNY and SUNY two- and four-year colleges
 - Doesn't cover room/board
- Income Thresholds:
 - 2017 - \$100K
 - 2018 - \$110k
 - 2019 - \$125k
- Begins Fall 2017
- Students must be enrolled full-time and average 30 credits per year to receive funding; plus must live in NY for 4 years after!



BUDGET: PROVISIONS THAT DIDN'T PASS

- Federal Sub-S Conformity
- Sales Tax “Marketplace Providers” Provision
- Centralized Administrative Hearings



TOPICS

PERSONAL INCOME TAX UPDATES AND HOT TOPICS

PERSONAL INCOME TAX HOT TOPICS

➤ Residency Audits Continue

- 5,000 per year
- \$250M+ revenue

➤ Two Tests

- Domicile
- Statutory Residency
 - Fallout continues from 2014 *Gaied* win

RESIDENCY – FACTS AND FIGURES

- **2016 NYC Comptroller Report: *The Increasing Concentration of High Income Taxpayers in the New York Economy***
 - 43% of US Taxpayers with income > \$10MM reported some NY source income
 - In 2014, *half* of NY taxpayers with > \$720K income were (or claimed to be) nonresidents!
 - Nonresidents earned more than \$90B in NY income in 2014 (\$68B in NYC alone)!
- **What could this mean?**
 - More audits? Are these folks really nonresidents?
 - Even more taxpayers? How many other non-filing nonresidents are there?
 - Re-birth of NYC nonresident tax?

STATUTORY RESIDENCY - MONAEO: TRACKING DAYS



PERSONAL INCOME TAX HOT TOPICS

➤ The “*Sobotka*” Issue (ALJ, September 2015)

- Change of domicile during tax year
- How does 183-day test apply?

➤ Flow-Thru Entity Issues

- Sales of partnership/LLC interests and real estate
- Difficult apportionment issues
 - S corps: follow corporate tax rules
 - LLCs/Partnerships: direct accounting or 3-factor

EMPIRE ZONE CASES: INCOME TAX

Matter of Purcell, Tax Appeals Tribunal, Nov. 14, 2016

- Tribunal held the tax department’s methodology for computing the “tax reduction credit” in the old Empire Zone Program was reasonable
- Tax department argued even though S corporation shareholders who were NY residents may have paid 100% tax on their S corp income, they could only get a credit for the amount of S corp income that was properly apportionable to NYS under the business allocation percentage rules that apply to *nonresident* shareholders
- Reverses several prior ALJ rulings

PERSONAL INCOME TAX CASES

Matter of Blatt, ALJ Determination, Feb. 2, 2017

- Division pushed the home factor because the taxpayer kept his apartment in NYC during the audit period, but ALJ said it's necessary to review the totality of the factors coupled with the taxpayer's stated intentions
- Given the taxpayer's lifestyle and employment circumstances, ALJ found the apartment didn't outweigh taxpayer's overall intention to move to Texas
- Steps the taxpayer took to change his domicile were in a logical and reasonable fashion, especially since he moved his dog with him, marking the ultimate change in domicile status

PERSONAL INCOME TAX CASES

Chamberlain v. NYS, New York State Supreme Court, March 3, 2017

- Taxpayers alleged NY's statutory residency scheme improperly subjected them to double taxation in violation of the Federal Commerce Clause
- Based on US Supreme Court's constitutional analysis in *Wynne v. Maryland*, where the Court struck down a portion of MD's resident credit scheme
- Court here held NY's scheme was constitutional despite the Supreme Court ruling – Court held *Wynne* didn't alter the constitutional analysis NY courts had used pre-*Wynne*, and that the tax passed the “internal consistency test” used in *Wynne*
- Case is on appeal.

WITHHOLDING AUDITS – FACTS AND FIGURES

**NY withholding
audit risk is
growing.**

395

NY payroll withholding audits
open/closed in 2015

150%

Audit \$ collected in 2015 vs. 2014

<30%

Companies effectively managing business travel risks

WITHHOLDING TAX AUDIT NUTS AND BOLTS

What do NY auditors look at?

- > Report 3-1: No Nexus, Federal Wages greater than \$20,000, NYS Wages greater than \$0 [why withholding?]
- > Report 3-2: No NYS Nexus & 0 Wages & 0 Withholding & Federal Wage greater than \$500,000 [high income earners]
- > Report 3-3: No NYS Nexus & Match Wage Reporting in at least one of the previous 5 years [bonus or deferred comp issue for nonresident?]
- > Report 7: Employees with NYS Zip or Address and No NYS Withholding
- > Report 14: NYS Work & No NYS Withholding & No NYS zip or address

TOPICS

SALES TAX UPDATES AND HOT TOPICS

TOP TEN SALES TAX AUDIT ISSUES

1. Cloud computing
 - Is it a license of software?
 - Is it a an information service? – *RetailData* and *Wegmans*
 - Is it the electronic delivery of other tangible property?
 - Remember allocation and overlapping audit rules.
2. Cheeseboard and consultants
3. Catering rules
4. Bulk sales rules (derivative liability)

TOP TEN SALES TAX AUDIT ISSUES (CON'T.)

5. Contractors
6. Info Services and Wall Street
7. Capital Improvements
8. Art Galleries
9. Cash businesses
10. Boats

SALES TAX CASES

Matter of CLM Associates, LLC, ALJ Determination, Feb. 23, 2017

- Transfer of titles to loaner cars from dealerships to the taxpayer constituted taxable retail sales
- Taxpayer was a holding company that owned several car dealerships (all single member LLCs), where loaner cars were acquired by the dealerships and then transferred and titled to the taxpayer – no cash changed hands. When customers used the loaner cars, expenses associated with this were allocated to the respective dealership
- ALJ found these were transfers for consideration, and found consideration included (i) benefit to dealerships to assumption of liability by the taxpayer and (ii) better administration/management of loaner program by consolidating those functions through the taxpayer
- Tax liability more than \$1 million, and all the cars were eventually sold by the dealerships

SALES TAX CASES

Matter of Stamford Subaru, LLC, Tax Appeals Tribunal, Nov. 23, 2016

- Automobile dealership located in CT about 3 miles from the NY border that frequently sold automobiles to NY residents, was denied a refund claim by NY for sales tax the taxpayer mistakenly remitted to NY instead of CT
- Taxpayer argued it collected sales tax, knowing it was payable to either NY or CT, but mistakenly sent it to NY – CT asked the taxpayer to correct the error, but NY denied the taxpayer's refund claim to NY
- Tribunal ruled that because the taxpayer hadn't actually repaid the tax to its customers it hadn't satisfied the repayment requirement, which the taxpayer argued was satisfied by assuming its customers' debts

SALES TAX CASES

Wegmans Food Markets, Inc., Tax Appeals Tribunal (3/10/2016)

- Pricing information obtained from products on the shelves of supermarkets open to the public that is subsequently customarily compiled and analyzed is not personal or individual in nature.
 - > Is this right?
 - > How would we view regular surveys or polling work now?

TOPICS

CORPORATE TAX UPDATES AND HOT TOPICS

CORPORATE TAX HOT TOPICS

- Into Year #3 of corporate tax reform
 - FAQs continue to be issued
 - Audits should be now starting
- Market-based sourcing: primary audit issue?
 - Example: change in NY apportionment for service company
- Intersection between economic nexus and market-based sourcing: non-NY service providers

CORPORATE TAX HOT TOPICS

➤ PNOL Conversion Subtraction

- Pre-2014 NOL pool available for 20 years (maximum 1/10 per year applied against apportioned business income) beginning in the 2015 tax year, unless two-year election made
- NYS has indicated that it will look closely at the calculation of the PNOL conversion subtraction and the statute of limitations will remain open to examine the original calculation. Taxpayers must complete for CT-3.3 to use PNOLs.

➤ Apportionment

- Complex apportionment form on the CT-3 and CT-3S requires separate apportionment of various categories of receipts
- NYS is issuing bills for additional tax due, computed using a 100% BAP, if the apportionment form is not properly filled out
- For S corporations, all receipts (including receipts from non-taxable investment and exempt income) go into the apportionment fraction

CORPORATE TAX HOT TOPICS

➤ Corporate Tax Reform: Draft Regulations

- NYS has issued draft regulations on nexus, apportionment, combined reporting, and discretionary adjustments
- Creates complex rules for apportioning 15 different categories of receipts, along with different rules and definitions for business vs. individual customers
- Creates high burden of “due diligence” for taxpayers to obtain information to properly source income and receipts, including corporate partners of partnerships
- Current draft of regulation permits Tax Department to use its discretionary authority if the statutory apportionment fraction does not “reach a fair result.”

NEXUS GENERALLY

➤ Definition

- “Connection”
- *Quill* still the law
 - For sales tax; but not for long?

➤ Economic Nexus

- NY’s \$1M Corp Tax Threshold – Effective 2015
- Other states looking to bright-line rules

CORPORATE TAX CASES

Matter of NRG, ALJ Determination, March 30, 2017

- ALJ found CoA decision in *James Square* does not prohibit treating a QEZE decertification as effective on January 1, 2009
- ALJ held in *James Square* taxpayer was subject to decertification based on “the retroactive application of a statute that specifically applied to prior tax years,” but the year at issue was 2009, so although enacted on April 7, 2009, the 2009 amendments were not a retroactive application of the law
- CoA in *James Square* said: “the 2009 Amendments should not be applied retroactively”

CORPORATE TAX CASES

Matter of Forest City (1), Tax Appeals Tribunal, May 19, 2016

- Tribunal reversed and remanded ALJ's determination ruling the taxpayer was not entitled to QEZE credits because it failed to prove any qualified employees to support an employment factor greater than 0
- Taxpayer alleged the employment number was 1 for the years at issue in its petition, and the Division filed its answer late – the Tribunal ruled the allegation should be “deemed admitted”
- Remand to the ALJ to determine amount of “eligible real property taxes” forming the base for the credit
- Taxpayer won on remand too!

TOPICS

COMPLIANCE/ENFORCEMENT UPDATES AND HOT TOPICS

OTHER ISSUES: COMPLIANCE AND ENFORCEMENT

- New compliance measures
- Driver's Licenses: suspensions and ID numbers!
- Increased criminal investigations
- CARP
- Whistleblowers: New Hedge Fund Case: \$40M recovery
 - Largest FCA tax settlement to date

HARBINGER CAPITAL CASE

- FCA case settled with NYS Attorney General on 4/3/2017 for \$40 million
 - State's Share: \$31.M
 - Relator's Share: \$8.8M
- Largest settlement to-date of tax claim under NYS False Claims Act
- Anonymous relator



THANK YOU



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