

REPORT ON EXECUTIVE BUDGET FY 2020

Hodgson Russ State & Local Tax Alert
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On April 1, Governor Cuomo announced that New York lawmakers passed the \$175.5 billion FY 2020 Budget (the “Final Bill”). The Final Bill (S. 1509-C / A. 2009-C) is available here. As of this writing, it has not been signed by the Governor. We have been following the evolution of the budget since Governor Cuomo released his proposal on January 15th, which we covered here. The tax and revenue highlights of the Final Bill, along with the omissions or differences from the Governor’s original proposals, are summarized below. Other aspects of the Final Bill, including criminal justice reform, MTA reforms, and changes to the Public Authority Law, are not discussed.

Income Tax Provisions:

- **Extension of Higher “Millionaires Tax” PIT Rates for Five Years (Part P).** The top New York State personal income tax bracket of 8.82% was scheduled to expire after 2019. The Final Bill immediately extends the top bracket through 2024.
- **Sourcing Rule for GILTI Apportionment (Part C).** Internal Revenue Code (“IRC”) § 951A(a) requires global intangible low-taxed income (“GILTI”), as defined by IRC § 951A(b)(1), to be included in federal gross income. To determine net GILTI, IRC § 250(a)(1)(B)i allows certain taxpayers a deduction for part of this income. Previously, New York did not have a rule for the net GILTI included in business income. The Final Bill establishes a statutory sourcing rule for GILTI by requiring the net GILTI to be included in the denominator of the apportionment factor, with zero in the numerator. Such treatment of GILTI mirrors the discretionary adjustment previously provided by the Commissioner and described in Form CT-3-1, *Instructions for Form CT-3*. A proposal to exclude 95% of GILTI from the income base looked like it would be included in the Final Bill, but was excluded at the last minute. The passed legislation will apply to taxable years beginning on or after January 1, 2018.
- **Extension of the PIT Limitation on Charitable Contribution Deductions for Five Years (Part Q).** The New York itemized charitable deduction is limited to 50% of the federal deduction for individuals with adjusted gross income (“AGI”) between \$1-10 million, and to 25% of the federal deduction for individuals with AGI over \$10 million. The 25% limitation for individuals with an AGI over \$10 million was set to expire at the end of 2019. The Final Bill has immediately extended the current 50% and 25% limitation structure through 2024 and made conforming amendments to NYC Administration Code § 11-1715(g).

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- **Extension of the e-File Mandate (Part A).** Tax Law § 29 requires tax preparers who meet certain criteria to e-file New York tax returns. See TB-MU-220 (Mar. 19, 2014). The e-filing mandate was originally enacted in 2008 and was set to expire after the 2019 tax year. The Final Bill has immediately extended the e-file mandate through 2024. The Governor's original proposal, however, would have made the mandate permanent.
- **Decouple from IRC Federal Basis for Q-NYS Manufacturing Test (Part D).** To determine whether a manufacturer is a qualified New York manufacturer—permitting a reduced business income base tax rate, a reduced tax rate and cap on the capital base, a lower fixed dollar minimum tax, and a manufacturer's real property tax credit—previous law applied a test referencing the federal adjusted basis of the taxpayer's manufacturing property in the state. In recognition of the fact that federal bonus depreciation might drive the basis of qualifying assets below the test's threshold, the Final Bill immediately amended Tax Law § 210(1)(a)(vi) and (b)(2) and New York City Administrative Code § 11-654(1)(k)(4)(ii) to apply the test by reference to New York State adjusted basis instead of the federal adjusted basis.
- **Exclusion from Entire Net Income of Certain Contributions to the Capital of a Corporation (Part X).** Effective December 22, 2017, the Tax Cuts and Jobs Act amended IRC § 118(b) to require that contributions by a governmental entity or civic group to a corporation's capital be included in the corporation's federal gross income. In New York, because of New York's federal conformity, this resulted in the inclusion of subsidies like Empire State Development grants in the recipient's entire net income. The Final Bill immediately restores favorable non-tax treatment of these contributions by amending Tax Law §§ 208(9)(a) and 1503(b) and NYC Administrative Code § 11-602(8)(a) to exclude from entire net income any contributions to the capital of a corporation by a governmental entity or civic group.
- **Inclusion of Certain NYS Gambling Winnings in Nonresident NYS Income (Part M).** The Final Bill amends Tax Law § 631(b) to include New York gambling winnings in excess of \$5,000 as taxable New York source income to New York nonresidents. The Final Bill also amends Tax Law § 671(b) to require withholding on gambling winnings in New York, when such winnings would be subject to withholding under IRC § 3402. Both amendments take place immediately and apply to taxable years beginning on or after January 1, 2019.

Sales Tax Provisions

- **Vendors May Advertise to Pay Sales Tax on Behalf of Customers (Part DDD).** Vendors required to collect and remit New York sales tax may now advertise to customers that the vendor will pay the sales tax imposed on behalf of the customer. In advertising, vendors must state on every bill, memorandum, receipt, or other statement of the price or amount paid both the amount of tax due and that the vendor will pay the tax imposed on the transaction. Vendors may begin making such advertisements immediately.
- **Adoption of Required Nexus for "Marketplace Providers" (Part G).** The Final Bill requires "marketplace providers" to collect sales tax on taxable sales that they facilitate. A marketplace provider is a person who, pursuant to an agreement with a marketplace seller, facilitates sales of tangible personal property by providing "a forum in which, or by means of which, the sale takes place or the offer of the sale is accepted, including a shop, store, booth, an internet website, catalog, or similar forum." Added since the Governor's proposal, however, is an amendment that establishes an applicability threshold for marketplace providers at \$300,000 in sales and 100 transactions during the prior four sales tax quarters. This section of the Final Bill takes effect immediately and applies to taxable years beginning on or after January 1, 2019.

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- **Elimination of Energy Services Sales Tax Exemption (Part H).** Previously, the effective tax rate on the transportation, transmission, and distribution of gas and electricity (TTD) had been reduced to zero when it was sold separately from the commodity. This effectively resulted in an exemption for these services provided in conjunction with energy sold by unregulated energy service companies (ESCOs). Under the Final Bill, with takes effect June 1, 2019, the sales tax exemption for separately-sold TTD has been eliminated.
- **Extension of Authority to Require Segregated Accounts for Delinquent Sales Tax Vendors (Part S).** Where the Tax Commissioner deems it necessary to protect sales tax revenues, a noncompliant or delinquent vendor may be required to deposit the sales tax it collects into a segregated account. Additionally, a 2011 amendment to Tax Law § 1137 authorized the Commissioner to debit segregated accounts, to require a vendor to deposit the sales tax moneys at least weekly, and to require the vendor to obtain a bond if the vendor failed to comply. Tax Law § 1134 was also previously amended to authorize the Commissioner to suspend or revoke a vendor's sales tax certificate of authority if the vendor did not comply with the segregated accounts program's requirements. The segregated accounts provision was set to expire in December 2019; however, the Final Bill will immediately extend the Tax Department's authority until December 2024. The Governor's proposal would have repealed the sunset date and allowed the current provision to remain in place indefinitely.

Property Tax Provisions:

- **Real Property Tax Cap (Part NNN).** The 2% property tax cap, which was originally implemented in 2012, is immediately made permanent. The Governor's office has said that New York taxpayers have saved approximately \$25 billion statewide since 2012 due to the cap.
- **Additional New York City Real Property Transfer Tax (Part OOO).** The Final Bill imposes additional real property transfer taxes, at \$1.50 per \$500 of sales price, applicable to residential properties valued at more than \$3 million and non-residential properties valued at more than \$2 million in New York City. The Final Bill, which takes effect July 1, 2019, also imposes an additional supplemental real property transfer tax on residential properties in New York City valued at over \$2 million, which tops out at 2.9% for properties sold for more than \$25 million.

Miscellaneous Provisions

- **Congestion Pricing Program for Vehicles Traveling Below 61st Street in Manhattan (Subpart A).** Although not expected to begin until 2021, the Final Bill establishes a six-person commission called the Traffic Mobility Review Board to determine the cost of driving below 61st Street in Manhattan. Potential price breaks and exemptions are yet to be determined.
- **Imposition of Opioid Excise Tax (Part XX).** The Final Bill imposes an excise tax on the first sale of opioids in New York State that takes effect July 1, 2019. However, unlike the Governor's proposal, the Final Bill does include amendments that exempt sales to hospice and chemical dependency programs.
- **Adoption of 20% Supplemental Tax on Vapor Products (Part UU).** Among other changes involving tobacco sales, the Final Budget includes an immediate 20% supplemental tax on sales of vapor products.
- **Tax Shelter Provisions Extended and Tax Preparer Penalties Updated (Part O).** Since 2005, taxpayers and advisors who are required to report tax shelter activity to the IRS must also report that activity to New York State. Penalties apply

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for nondisclosure and underpayment of taxes related to participation in certain transactions. The Final Bill immediately extends these tax shelter reporting and penalty provisions for five years, through 2024. The Governor had proposed a permanent extension of the reporting and penalty provisions. In addition, the Final Bill immediately updates the Tax Law to: (1) clarify the penalties against preparers who take positions on returns or claims that are not properly supported by the tax law and (2) ensure that penalties for failing to sign a return and for failing to provide a required identification number on a return apply to all tax preparers.

- **Exemptions for Suspensions of Driver’s Licenses (Part EEE).** The Final Bill immediately amends existing Tax Law provisions that result in the suspension of driver’s licenses based on tax delinquencies. The amendments exempt persons receiving public assistance or who can demonstrate that suspension will cause undue financial hardship. No similar provision was originally included in the Governor’s proposal.
- **Creation of New York State Employer-Provided Child Care Credit (Part L).** Under IRC § 45F, employers are allowed a federal credit for qualifying expenditures paid or incurred in providing child care alternatives for their employees. This Final Bill in the form of a credit equal to 25% of qualified child care expenditures related to an employer-provided child care facility located in New York plus 10% of qualified child care resources and referral expenditures, provides a similar state tax credit for New York employers. Like the federal credit, the New York credit, which applies to taxable years beginning or after January 1, 2020, is capped at \$150,000 per employer, per taxable year.

Some provisions of the Governor’s January 2019 proposals were ultimately **omitted** from the Final Bill (and other provisions that popped up later eventually went away). Some of the noteworthy omissions are discussed below:

- **New York City Pied-a-Terre Tax.** Although not actually included in the Governor’s original proposal, there was much buzz around a potential real property tax on non-primary residences located in New York City with a market value of \$5 million or more. The Senate and Assembly budget proposals included such taxes with tax rates ranging from 0.5% to 4% on properties valued at \$25 million or more.
- **Close the Carried Interest “Loophole”.** Federal tax treatment allows hedge fund managers and private equity investors to treat carried interest income as capital gains, rather than ordinary income. New York is unable to tax such capital gain income when earned in New York by a nonresident. Mirroring a similar proposal from the Governor’s FY 2019 proposals, the Governor again proposed a requirement that all income from investment management services to be treated, for New York purposes, as income earned from a trade or business and would subject the gain to an additional 17% carried interest “fairness” fee. However, the proposal bill dealing with carried interests would have taken effect only if Connecticut, New Jersey, Massachusetts, and Pennsylvania enacted legislation having a substantially similar effect.
- **Enact the Cannabis Regulation and Taxation Act.** The Governor had proposed a bill for a new Cannabis Regulation and Taxation Act. High points of the proposal included provisions to legalize the adult use of marijuana along with the availability of hemp products, and to expand the State’s current medical marijuana program. The proposal would have also added a new article to the Tax Law—Article 20-C, titled “Tax on Adult-Use Cannabis Products”—which would have imposed three new taxes: first, a tax on the cultivation of cannabis at the rate of \$1 per “dry-weight gram of cannabis flower” and \$0.25 per “dry-weight gram of cannabis trim;” second, a state-level tax on the sale by a wholesaler to a retail dispensary at the rate of 20% of the invoice price; and third, a county-level tax on the sale by a wholesaler to a retail dispensary at the rate of 2% of the invoice price. In addition, all wholesalers would have been required to apply for

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and obtain a Certificate of Registration from the New York State Tax Department before starting business and the registration would have been renewable every two years.

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