

TAX PROVISIONS OF INTEREST IN THE PROPOSED 2023-24 BUDGET BILL

Hodgson Russ State & Local Tax Alert
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Here are some highlights from the New York State Legislature's proposed Revenue portions of the State's 2023-24 Budget (Assembly Bill 3009/Senate Bill 4009)(the "Budget").

Clarification of the Treatment of Limited Partners for the Metropolitan Commuter Transportation Mobility Tax ("MCTMT"): For those unfamiliar with the MCTMT, it is a tax imposed on certain employers and self-employed individuals engaging in business within the metropolitan commuter transportation district (MCTD), which includes the counties of New York, Bronx, Kings, Queens, Richmond, Rockland, Nassau, Suffolk, Orange, Putnam, Dutchess, and Westchester. The MCTMT applies to employers paying wages to employees in the MCTD and to self-employed individuals (including partners) with net earnings from sources within the MCTD that exceed \$50,000. The Budget (at Part B) would amend the definition of "net earnings from self-employment" in the Tax Law to clarify the treatment of limited partners who are actively engaged in the operations of the partnership for purposes of the MCTMT. Currently, the definition references the Internal Revenue Code ("IRC"), which defines "net earnings from self-employment" and exempts amounts earned by limited partners from self-employment tax. This amendment to the Tax Law would restrict the definition of a "limited partner" for the MCTMT to exclude limited partners who actively participate in the partnership. The language of the amendment states that for purposes of determining whether the exclusion applies: "an individual shall not be considered a limited partner if the individual, directly or indirectly, takes part in the control, or participates in the management or operations of the partnership such that the individual is not a passive investor, regardless of the individual's title or characterization in a partnership or operating agreement." The changes would take effect immediately when the Budget is signed into law.

According to the Memorandum in Support of the Budget bill, "this *clarifying* amendment would provide that only true limited partners are not subject to the MCTMT." Referring to the change as a "clarification" opens the door for the Department of Taxation and Finance to impose the change retroactively, which would likely be unconstitutional. And the proposal does not explicitly provide that the law would not be retroactively applied to limited partners that engaged in participation of the management or operations of a partnership. Therefore, taxpayers

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who in prior years were limited partners and were lawfully not paying the MCTMT could suddenly be subject to potential tax liability for all open tax years. For taxpayers who reasonably relied on the law as previously written, such a retroactive application of the change would likely be found to be unconstitutional.

MCTMT Rate Increase: A provision of a different bill (Part Q, A. 3008/S. 4008) proposes to increase the rate of the MCTMT from 0.34% to 0.50% for employers with quarterly payrolls over \$437,500 (effective July 1, 2023), and from 0.42% to 0.50% for taxpayers with MCTD-source earnings from self-employment (effective January 1, 2024).

PTET Technical Changes: Part J (Subpart C) of the Budget proposes changes to the State Pass-Through Entity Tax (PTET) and the City PTET. It would amend the definitions of “pass-through entity taxable income” and “city pass-through entity taxable income” in Tax Law §§ 860(h) and 867(b) to require entities to exclude deductions for PTET taxes paid when computing their state and city pass-through entity taxable incomes. This would correct an unintended “circular” mathematical computation under current law requiring entities to deduct certain taxes paid from their pass-through entity taxable income, including the pass-through entity tax. In addition, Part J (Subpart C) would amend the definition of “city taxpayer” to correct the unintentional omission of city resident trusts and estates from participating in the NYC PTET. Lastly, this part would clarify when an entity must elect into/revoke their election into the PTET and NYC PTET.

Cigarettes and Tobacco Products: Part S of the Budget would increase the excise tax on cigarettes in New York by \$1.00. The current excise tax rate on a package of 20 cigarettes sold in New York State is \$4.35. The Budget proposes to increase this rate by \$1.00, for an excise tax rate of \$5.35 for each package of 20 cigarettes. The Budget would also increase the existing use tax rate on cigarettes by the same amount. Finally, the Budget would require that any tax due on account of the increased rate on any cigarettes possessed for sale in the State, as of the close of business on August 31, 2023, must be paid by November 20, 2023.

In addition, the Budget would amend the Tax Law to provide for the imposition of a civil penalty for refusal to comply with cigarette and tobacco inspections. The Tax Law currently authorizes the Department of Taxation and Finance (DTF) to conduct regulatory inspections of retail tobacco dealers, but it does not specifically address the consequences of refusal to allow a regulatory inspection. The Budget would explicitly provide that a retail dealer who refuses an inspection would be subject to a one-year suspension of its certificate of registration to sell cigarettes and tobacco products. For a second such refusal within three years, the retail dealer’s certificate of registration would be permanently revoked. The Budget also proposes to establish penalties for inspection refusal by a retail dealer who does not possess a valid registration because it never obtained one or because its registration was suspended or revoked at the time of refusal. In such circumstances, the Budget would set a penalty of up to \$5,000 for the first refusal and up to \$10,000 for a second refusal within three years.

Credits: The Budget contained a number of credit provisions. Below is a list of credits that would be created, extended, or modified by the Budget:

Creation of new credits/exemptions: Tax Credit for Child Care Creation and Expansion (Part G); New York City Biotech Tax Credit (Part H).

Extension/modification of existing credits/exemptions: The following credits/exemptions would be extended, modified, and/or enhanced: Investment Tax Credit for Farmers (Part C); Film Tax Credit (Part D); COVID-19 Capital Costs Tax Credit Program (Part F); Rehabilitation of Historic Properties Tax Credit (Part I); Empire State Commercial Production Tax

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Credit (Part I); No. 6 Heating Oil Conversion Tax Credit (Part I); New York City Musical and Theatrical Production Tax Credit (Part I); Disabled Transportation Tax Credit (Part J); Brownfield Redevelopment Tax Credit (Part J); Senior Citizens Real Property Tax Exemption (Part K).

Business Income Tax Rate Extension: Part I of the Budget proposes to extend certain tax rates through tax year 2026, including the current 7.25% income tax rate for corporate taxpayers with business income bases in excess of \$5 million, and the current 0.1875% capital base tax. The higher income tax rate and capital base tax were scheduled to sunset at the end of 2023.

Elimination of the Congestion Surcharge Registration Requirements: Based on recent changes in the Tax Law, the congestion surcharge registration requirement has been determined to be unnecessary (Part P). Therefore, the Budget would eliminate the registration requirement.

Changes to Vending Machine Sales Tax Exemption: The Budget, at Part R, would extend an existing sales tax exemption for certain food and drink purchased from vending machines, but only for vending machines operated by participants in the Business Enterprise Program (“BEP”). Currently, purchases up to \$1.50 of certain food and drink items from vending machines that accept only coin or currency are exempt from sales tax, while purchases up to \$2.00 from vending machines that are capable of accepting payment in a form other than coin or currency (“cashless” purchases) are exempt from sales tax regardless of whether that vending machine also accepts coin or currency. The current exemption is effective through May 31, 2023. The Budget would extend the exemption through May 31, 2024, but limit it to BEP participants.

Make Local Sales Tax Rate Authorizations Permanent: Part O of the Budget proposes to make permanent certain cities and counties’ ability to impose increased sales and use tax rates. This part would also preserve the current revenue distribution scheme with respect to such additional rates and eliminate the need for those counties and cities to periodically obtain approval through the state legislative process.

State and Federal S Corporation Conformity: The Budget (Part CC) offers amendments to various provisions within the Tax Law to provide that all federal S corporations would be automatically treated as S corporations for New York tax purposes unless the corporation is a qualified New York manufacturer under Tax Law § 210(1)(a)(vi) and chooses New York C corporation status on its tax return. This change would take effect for tax years beginning on or after January 1, 2024.

Disaster Relief

Interest Abatement for Taxpayers Impacted by Declared Disasters: Part A of the Budget would expand the Commissioner’s authority to provide relief to taxpayers affected by a presidentially-declared disaster or by a disaster emergency declared by the Governor, allowing the Commissioner to abate any interest that has accrued for the period during which taxpayers were unable to meet a tax deadline due to impacts of these disasters.

Abatement of Penalties for Underpayment of Estimated Tax by a Corporation: The Budget, in Part E, would allow the Commissioner to waive or reduce the penalty for underpayment of estimated tax by a corporation impacted by casualty, disaster, or other unusual circumstances, creating parity in this respect between the corporate and personal income tax underpayment penalties.

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Miscellaneous

Extend the Oil and Gas Fee: Part L of the Budget proposes to extend the expiration date of Real Property Law § 593, which sets forth a schedule of fees to recover the cost of setting “unit of production” values for the oil and gas industry, from March 31, 2024, to March 31, 2027.

Extend Reduced Transfer Tax Rates for Qualifying REITs for Three Years: Part U of the Budget would extend the reduced tax rates for real estate investment trusts under the New York State real estate transfer tax and the New York City real property transfer tax for conveyances for three years until September 1, 2026.

Clarification of the Wind and Solar Energy Valuation Model: The Budget would clarify that the Department of Taxation and Finance’s adoption of the solar and wind energy system appraisal model for real property tax is not subject to the State Administrative Procedure Act (SAPA) in Part N.

Amend Motor Fuel Reporting Designation: Part Q of the Budget proposes to require distributors of motor fuel and Diesel motor to collect, report, and remit taxes to the Department of Taxation and Finance on the sale of any gallon of fuel, including additional gallons resulting from temperature fluctuations. In the past, distributors would collect additional tax on the fuel due to temperature fluctuations, but not remit additional tax.

Allow Department of Tax and Finance the Right to Appeal Tax Appeals Tribunal Decisions: Under Part V of the Budget the Department of Taxation and Finance would be able to appeal Tax Appeals Tribunal decisions, like a taxpayer, by petitioning the Appellate Division of the Supreme Court, Third Department.