

Summary of Corporation Tax Legislative Changes Enacted in 2003

This memorandum contains brief summaries of the corporation tax legislative changes (Chapters 62 and 63 of the Laws of 2003) enacted in 2003.

New York S corporation franchise tax changes (Article 9-A)

The Tax Law has been amended to change the franchise tax imposed on New York S corporations. Prior to the amendment, a New York S corporation was subject to the franchise tax computed on the higher of the tax on the entire net income (ENI) base or the fixed dollar minimum tax, reduced by the Article 22 tax equivalent. Also, for a termination year, the tax for a New York S corporation short year was the tax on the ENI base less the Article 22 tax equivalent, calculated without regard to the fixed dollar minimum tax (TSB-M-90(11)C).

For tax years beginning in 2003, 2004, and 2005, for a New York S corporation, the Tax Law has been amended to eliminate the tax on the ENI base and impose only the fixed dollar minimum tax, as prescribed in section 210(1)(d) of the Tax Law. For a termination year, the tax for a New York S corporation short year is the fixed dollar minimum tax. Accordingly, for tax years beginning in 2003, 2004, and 2005, a New York S corporation is subject to the applicable fixed dollar minimum tax as follows:

| For a New York S corporation with a gross payroll of: | Fixed dollar minimum tax equals: |
|--|----------------------------------|
| \$6,250,000 or more | \$1,500 |
| More than \$1,000,000 but less than \$6,250,000 | \$425 |
| More than \$500,000 but not more than \$1,000,000 | \$325 |
| More than \$250,000 but not more than \$500,000 | \$225 |
| \$250,000 or less | \$100 |
| However, if the New York S corporation's gross payroll, total receipts, and average value of gross assets are each \$1,000 or less*: | \$800 |

*If a tax year is less than 12 months, compute the gross payroll and total receipts by dividing the amount of each by the number of months in the short year and multiplying the result by 12.

(Tax Law section 210(1)(g)(1))

Bank tax extender (Article 32)

The tax provisions that were scheduled to expire for tax years beginning on or after January 1, 2003, have been extended for two years.

Transitional provisions for the federal Gramm-Leach-Bliley Act extended (Articles 9-A and 32)

The tax provisions that were scheduled to expire for tax years beginning on or after January 1, 2003, have been extended for one year. For more information on the provisions that were extended, see page 6 of TSB-M-02(1)C, *Summary of Legislative Changes Enacted in 2001*.

Minimum interest rate reduced (Articles 9, 9-A, 32, and 33)

Sections 171, twenty-sixth(a) and 1096(e) of the Tax Law were amended to remove the fixed minimum interest rate payable on overpayments of tax. Previously, the minimum rate of interest payable on overpayments of tax was 6%. Under the new law, the rate is the sum of the federal short-term interest rate as provided under section 1096(e)(3) of the Tax Law plus two percentage points. This provision takes effect on October 1, 2003, for interest allowable and due on refunds or any other amounts that remain or become overpaid on or after October 1, 2003.

(Tax Law, sections 171, twenty-sixth(a) and 1096(e)(1))

Filing fees for limited liability companies and limited liability partnerships (Article 22)

Domestic and foreign limited liability companies that are treated as partnerships for federal income tax purposes, limited liability partnerships subject to Article 8-B of the Partnership Law and foreign limited partnerships, that have any income derived from New York sources as defined in Tax Law section 631 of the personal income tax, are required to file returns with the department and pay a filing fee with the return. Effective for tax years beginning on or after January 1, 2003, the prescribed filing and payment is due within 30 days of the last day of the tax year.

In addition, effective for tax years beginning in 2003 and 2004, the filing fees imposed have been increased. The amount of the filing fee has been increased to \$100 multiplied by the total number of members or partners of the limited liability company, limited liability partnership, or foreign limited partnership. The minimum amount of the fee has been increased to \$500 and the maximum amount of the fee has been increased to \$25,000.

Also, effective for tax years beginning in 2003 and 2004, single member limited liability companies that have income from New York State sources and are treated as disregarded entities for federal income tax purposes are subject to a return filing requirement and a filing fee. The fee is \$100 for each entity. The return and payment are due within 30 days of the last day of the tax year.

(Tax Law, section 658(c)(3))

Estimated tax payments required by partnerships, limited liability companies, and New York S corporations (Article 22)

Effective for tax years ending after December 31, 2002, a partnership, limited liability company that is treated as a partnership for federal income tax purposes, and New York S corporation, that has income from New York sources, is required to pay estimated taxes on behalf of its C corporation partners or members, and nonresident individual partners, members, or shareholders on their distributive or pro rata share of the respective entity's income. Estimated tax for nonresident individual partners and shareholders means a partner's or shareholder's distributive share or pro rata share of the entity's income derived from New York sources for the year less the partner's or shareholder's share of certain partnership related deductions allocated to New York State, multiplied by the highest rate of tax under section 601 of the Tax Law for the year (e.g., 7.7% for 2003). Estimated tax for corporate partners means a corporate partner's distributive share of the partnership's income derived from New York sources for the year multiplied by the highest rate of tax under section 210.1(a) of the Tax Law for the year (e.g., 7.5% for 2003). This amount is reduced by the partner's distributive share or shareholder's pro rata share of any allowable credits from the partnership or New York S corporation.

Further details will be addressed in a future TSB-M since this provision is the subject of pending legislation.

Visit the Tax Department's Web site at www.nystax.gov for Tax Law changes that may have occurred after this TSB-M was printed.

(Tax Law, sections 658(c)(4), 685(c) and 686(i))

Entire net income (ENI) modifications (Articles 9-A, 13, 32, and 33)

Modification for sport utility vehicle deduction (Article 9-A)

For tax years beginning on or after January 1, 2003, in determining ENI, taxpayers, except an eligible farmer, must add to federal taxable income the amount deducted under Internal Revenue Code (IRC) section 179 for a sport utility vehicle that weighs in excess of 6,000 pounds. IRC section 179 relates to an election to expense certain depreciable assets used in an active trade or business. An eligible farmer is a taxpayer who qualifies as an eligible farmer for purposes of the New York State farmers' school tax credit.

A related modification has been added to allow a subtraction for any recapture amount included in federal taxable income pursuant to IRC section 179(d) attributable to the federal deduction for a sport utility vehicle as described above. The modification may be made only for a vehicle for which the addition modification described above was made in the current year or a prior tax year.

Since the Tax Law does not contain a provision for depreciation for a sport utility vehicle in lieu of IRC section 179, amounts required to be added to federal taxable income are not allowed as a deduction in computing ENI in subsequent years. As such, the IRC section 179 expense benefit is permanently lost in computing ENI.

Additionally, no modification was made to the Tax Law to adjust any gain or loss for federal income tax purposes upon the subsequent sale or disposition of the property subject to the addition modification. As such, no adjustment is made to the federal gain or loss in computing ENI.

For purposes of these modifications, a sport utility vehicle means any four wheeled passenger vehicle which is manufactured primarily for use on public streets, roads, and highways. However, such term does not include (1) any ambulance, hearse or combination ambulance-hearse used by the taxpayer directly in a trade or business; (2) any vehicle used by a taxpayer directly in the trade or business of transporting persons or property for compensation or hire; or (3) any truck, van, or motor home. A truck is defined as any vehicle that has a primary load carrying device or container attached, or is equipped with an open cargo area or covered box not readily accessible from the passenger compartment.

(Tax Law, sections 208.9(a)(16) and 208.9(b)(16))

Modification for decoupling from federal bonus depreciation (Articles 9-A, 32, and 33)

Modifications to federal taxable income are required for property placed in service on or after June 1, 2003, that qualified for the special bonus depreciation allowance created by the federal *Job Creation and Worker Assistance Act of 2002*, and enhanced by the federal *Jobs and Growth Tax Relief Reconciliation Act of 2003*, and for which this allowance was claimed for federal income tax purposes. These modifications apply to qualified property other than (1) qualified resurgence zone property, and (2) qualified New York Liberty Zone property described in IRC section 1400L(b)(2) (without regard to subparagraph (C)(i) of such paragraph).

For tax years beginning on or after January 1, 2003, in computing ENI, a taxpayer must add to federal taxable income the amount of the depreciation deduction for qualified property allowable under IRC section 167. Also, a taxpayer must subtract from federal taxable income the depreciation deduction for qualified property allowable under IRC section 167 as if the property did not qualify for federal bonus depreciation provisions under IRC section 168(k)(2).

Qualified resurgence zone property means qualified property described in IRC section 168(k)(2) substantially all of the use of which is in the resurgence zone in the active conduct of a trade or business by the taxpayer in the zone, and the original use in the zone commences with the taxpayer on or after January 1, 2003.

The *resurgence zone* means the area of New York County bounded on the south by a line running from the intersection of the Hudson River with the Holland tunnel, and running from there east to Canal Street, then running along the centerline of Canal Street to the intersection of the Bowery and Canal Street, running from there in a southeasterly direction diagonally across

Manhattan Bridge Plaza, to the Manhattan Bridge and along the centerline of the Manhattan Bridge to the point where the centerline of the Manhattan Bridge would intersect with the easterly bank of the East River, and bounded on the north by a line running from the intersection of the Hudson River with the Holland Tunnel and running from there north along West Avenue to the intersection of Clarkson Street then running east along the centerline of Clarkson Street to the intersection of Washington Avenue, then running south along the centerline of Washington Avenue to the intersection of West Houston Street, then east along the centerline of West Houston Street, then at the intersection of the Avenue of the Americas continuing east along the centerline of East Houston Street to the easterly bank of the East River.

For tax years beginning on or after January 1, 2003, upon disposition of property to which the above addition or subtraction modification applies, the amount of any gain or loss includible in ENI must be adjusted to reflect the addition or subtraction modifications made pursuant to sections 208.9(a)(17) and 208.9(b)(17) under Article 9-A of the Tax Law, sections 1453(b)(13) and 1453(e)(17) under Article 32, or sections 1503(b)(1)(R) and 1503(b)(2)(T) under Article 33.

These new modifications will apply only to tax years beginning after 2002, and only to property placed in service on or after June 1, 2003.

(Tax Law, sections 208.9(a)(17), 208.9(b)(17), 208.9(o), 208.9(p), 208.9(q); 1453(b)(13), 1453(e)(17), 1453(r), 1453(s), 1453(t); 1503(b)(1)(R), 1503(b)(2)(T), 1503(b)(14), 1503(b)(15), and 1503(b)(16))

Related party modifications (Articles 9-A, 13, 32, and 33)

For tax years beginning on or after January 1, 2003, in computing ENI or other applicable tax base, taxpayers are required to modify federal taxable income with respect to certain royalty payments made with respect to the use of intangible property by a related member or members or royalty payments received from a related member or members. Taxpayers are also required to modify federal taxable income with respect to certain interest payments made to a related member or members or interest payments received from a related member or members.

Further details will be addressed in a future TSB-M, since this provision is the subject of pending legislation.

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(Tax Law, sections 208.9(o), 292(a)(6), 1453(r), and 1503(b)(14))

Attorney-in-fact (AIF) deduction (Article 9-A)

The Tax Law provides an attorney-in-fact (AIF) for a reciprocal insurer or a mutual insurance company that is an interinsurer with a subtraction from federal taxable income in computing ENI, if the reciprocal insurer or interinsurer has made the election provided for under

Internal Revenue Code section 835. Effective for tax years beginning on or after January 1, 2003, the Tax Law has been amended to provide an additional condition that must be met before the subtraction can be taken. The additional condition is that the reciprocal insurer or interinsurer must be subject to the additional franchise tax on insurance corporations imposed under section 1510(a) of the Tax Law. For tax years beginning on or after January 1, 2003, a reciprocal insurer or interinsurer is no longer subject to tax under section 1510(a). Accordingly, for tax years beginning on or after January 1, 2003, the subtraction is not allowed.

(Tax Law section 208.9(a)(15))

Franchise Tax on Insurance Corporations (Article 33)

Tax on non-life insurance corporations

For tax years beginning on or after January 1, 2003, non-life insurance corporations are no longer subject to the franchise tax imposed under sections 1501 and 1510 of the Tax Law. Instead, non-life insurance corporations are subject to a franchise tax imposed under section 1502-a of the Tax Law, based solely on gross direct premiums, less return premiums. Gross direct premiums, less return premiums, are taxed at the rate of 2%, except accident and health premiums, which are taxed at the rate of 1.75%. In no event may the tax imposed under section 1502-a of the Tax Law, before the application of tax credits, be less than \$250. Non-life insurance corporations are no longer required to file either Form CT-33 or Form CT-33-A, which have been renamed *Life Insurance Corporation Franchise Tax Return* and *Life Insurance Corporation Combined Franchise Tax Return*, respectively. Instead, these corporations are required to file Form CT-33-NL, *Non-life Insurance Corporation Franchise Tax Return*.

(Tax Law, section 1502-a)

Tax on life insurance corporations

Life insurance corporations remain subject to the franchise tax imposed under section 1501 of the Tax Law and the additional franchise tax imposed under section 1510 as these sections are limited by section 1505 of the Tax Law. However, for tax years beginning on or after January 1, 2003, in no event may the tax on life insurance corporations, computed prior to the application of any tax credits, be less than 1.5% of the premiums subject to tax under section 1510 of the Tax Law. Life insurance corporations are required to file either Form CT-33 or Form CT-33-A, which have been renamed *Life Insurance Corporation Franchise Tax Return* and *Life Insurance Corporation Combined Franchise Tax Return*, respectively.

(Tax Law, section 1505(b))

Metropolitan Commuter Transportation District (MCTD) allocation percentage for non-life insurance corporations

For tax years beginning on or after January 1, 2003, the MCTD allocation percentage for non-life insurance corporations is calculated by (1) dividing the direct premiums subject to tax under

section 1510 that are written on risks located or resident in the MCTD, by (2) the direct premiums subject to tax under section 1510 that are written on risks located or resident in New York State. MCTD direct premiums include premiums that are written, procured, or received in the MCTD on business that cannot be specifically assigned as located or resident in an area of New York State outside the MCTD, or in another state(s).

(Tax Law, section 1505-a(2))

New deduction for certain reinsurance premiums for life and non-life insurance corporations and captive insurance companies

Effective for tax years beginning on or after January 1, 1990, section 1510(c) of Article 33 of the Tax Law has been amended to allow a deduction from gross direct premiums for certain reinsurance premiums received from insurers not authorized by the Superintendent of Insurance to transact business in this state. For additional information, refer to TSB-M-03(3)C, *New Deduction Under Article 33 of the Tax Law for Certain Reinsurance Premiums, and Limited Opportunity for Refund of Tax Paid on These Premiums*; and TSB-M-03(3.1)C, *Correction to TSB-M-03(3)C, New Deduction Under Article 33 of the Tax Law for Certain Reinsurance Premiums, and Limited Opportunity for Refund of Tax Paid on These Premiums*.

(Tax Law, section 1510(c)(3)(B))

Surcharge retaliatory tax credit for both life and non-life insurance corporations

For tax years beginning on or after January 1, 2003, the four million dollar limitation on the total amount of the surcharge retaliatory tax credit claimed in any surcharge taxable year has been repealed. For additional information, refer to Form CT-33-M, *Insurance Corporation MTA Surcharge Return*.

(Tax Law, section 1505-a(d))