TSB-M-96-(1)C
Corporation Tax
November 6, 1996

Important Notice

Summary of 1996 Corporation Tax Law Changes

Business Corporation Franchise Tax

The Tax Law has been amended to provide business corporations with a check-off box to donate gifts to the Breast Cancer Research and Education Fund. Any contribution to this fund will not reduce the amount of state tax owed by the taxpayer. The provisions of this new section are applicable for taxable years beginning after 1995. (Chapter 279, Laws of 1996)

Railroad and Trucking Corporations

The rate of tax under section 184 of the Tax Law (Article 9 - Additional Franchise Tax on Transportation and Transmission Corporations and Associations) is decreased from .75 percent to .6 percent of the gross earnings of railroad and trucking companies, effective for taxable years beginning in or after 1997. Additionally, effective January 1, 1998, railroad and trucking companies will be subject to tax under Article 9-A of the Tax Law (Franchise Tax on Business Corporations) rather than Article 9. In the case of a calendar year taxpayer, its first Article 9-A year will be calendar 1998. In the case of a corporation which has a fiscal year for federal income tax purposes ending during 1998, its first Article 9-A year will be from January 1, 1998 to the date its federal fiscal year ends. Railroad and trucking companies, however, may elect to remain taxable under Article 9. This election must be made by March 15, 1998. (Chapter 309, Laws of 1996)

Credit For Rehabilitation Of Historic Barns

The investment tax credit under Article 9-A, the business corporation franchise tax, has been expanded to include expenditures paid or incurred for the rehabilitation of certain historic barns. The amount of the credit is 25 percent of the taxpayer's "qualifying rehabilitation expenditures" paid or incurred for any barn located in New York State that is a "qualified rehabilitated building." For purposes of this credit, a barn is a building originally designed and used for storing farm equipment or agricultural products or for housing livestock, but does not include barns converted to residential purposes, or barns where the historical appearance is materially altered by the rehabilitation. "Qualified rehabilitation expenditures" do not include any expenditures that are included in the computation of the regular investment tax credit.

The definitions of the terms "qualified rehabilitation expenditures" and "qualified rehabilitated building" are contained in Internal Revenue Code Section 47(c) (2) and Section 47(c) (1), respectively. The expenditures must qualify for the federal rehabilitation credit described in Section 47 of the Code. In general, under the federal provisions, a taxpayer may claim a credit equal to a specified percentage of its "qualified rehabilitation expenditures" incurred to substantially rehabilitate a qualifying structure. The expenses must, among other things, be properly chargeable to a capital account for property for which depreciation is allowable. The building that is being rehabilitated must have been placed in service before the commencement of the rehabilitation work, and it either must be a certified historic structure or must have been first placed into service before 1936. A building will be considered to be substantially rehabilitated if the expenditures incurred during the 24-month period selected by the taxpayer and ending with or within the taxable year exceed the greater of the adjusted basis of the building or $5,000. Under certain circumstances, the rehabilitation work may extend over a number of taxable years.

This credit is effective for taxable years beginning in or after 1997. (Chapter 309, Laws of 1996)

Farmers' School Property Tax Credit

A refundable credit under Article 9-A is available for taxpayers which are eligible farmers. This credit is effective for taxable years beginning in or after 1997. The credit is allowed against the franchise tax. The amount of the credit is the amount of school district real property taxes paid on qualified farmland and buildings, subject to certain acreage and income limitations.

An eligible farmer is a taxpayer whose federal gross income from farming is at least two-thirds of its federal gross income from all sources for the taxable year. The school district property tax upon which the credit is based is the tax paid on land, land improvements, structures and buildings used in agricultural production, located in New York State and owned by the taxpayer. Buildings used for the taxpayer's residential purpose are excluded. The credit is limited when the land exceeds the base acreage. The base acreage is defined as 100 acres for tax years beginning in 1997, 175 acres for tax years beginning in 1998 and 250 acres for tax years beginning in or after 1999. When the base acreage is exceeded, the allowable acreage is the base acreage plus 50 percent of the acreage in excess of the base acreage.

Example: A calendar year taxpayer is an eligible farmer primarily engaged in farming. The corporation owns 250 acres of property in 1997 that is used in agricultural production. The school tax paid on this property for 1997 was $3,000. The allowable acreage for the credit is the base acreage of 100 acres plus 50 percent of the acreage in excess of the base acreage (50% X [250-100]= 75 acres). The allowable acreage is therefore 100 acres + 75 acres = 175 acres. The credit is then computed by multiplying the school tax paid for the entire 250 acres by a ratio, the numerator of which is the allowable acreage of 175 acres and the denominator of which is the total acreage of 250 acres (175/250 = 70 percent). The amount of the credit allowable is $3,000 X 70% or $2,100.

If two or more related parties own qualified agricultural property on March first of the tax year, the base acreage must be split among the parties. A related party, as to the taxpayer, means another corporation subject to tax under Article 9-A, where the taxpayer and the corporation are members of the same controlled group as defined in section 267(f) of the Internal Revenue Code. A related party also includes a stockholder who owns more than 50 percent of the taxpayer corporation. A related party also includes another business (partnership, other corporation, etc.) where the same person owns more than 50 percent of the other business. A related party also includes another business, such as a partnership, of which the taxpayer corporation owns more than 50 percent. The related party rules also take into account some forms of indirect stock ownership. For example, a married individual is deemed to own the corporation stock owned by his or her spouse, and a partner in a partnership is deemed to own a proportionate share of any corporation stock owned by the partnership. The base acreage must be divided equally among the taxpayer and the related parties unless the taxpayer and the related parties consent to an unequal division. Any unequal division of the base acreage must be made on the tax return of the first related party to file and claim the credit. A schedule must be attached that describes how the base acreage is divided and the schedule must be signed by the taxpayer and the related parties. A copy of this schedule must be attached to the tax return of each related party claiming the credit. A different division of the base acreage can be elected by the related parties each year. If there is no schedule attached to a return, an equal division of base acreage will be assumed.

The credit is also phased out between $100,000 and $150,000 of entire net income. The credit is reduced to zero when entire net income exceeds $150,000. In the event that the entire net income of the taxpayer exceeds $100,000, the allowable school district property tax is the school tax paid reduced by the product of the amount of such tax and a percentage. The percentage is determined by multiplying one hundred percent by a fraction, the numerator of which is the lesser of $50,000 or the excess of the taxpayer’s entire net income over $100,000 and the denominator of which is $50,000.

Example: In 1997, a corporation pays $30,000 in school district property tax on qualified agricultural property. The acreage limitation does not apply. If the corporation’s entire net income for 1997 is $100,000 or less, the credit of $30,000 is allowed in full. If the corporation’s entire net income is $150,000 or more, no credit is allowed. If the corporation’s entire net income is $120,000, the credit is reduced by the proportion that the income in excess of $100,000 ($20,000) is to $50,000. In this case the credit is reduced by 40 percent ($20,000 divided by $50,000), meaning that 60 percent of the credit, or $18,000, is allowed.

If the credit exceeds the tax due, it may not be used to reduce the tax payable to less than the higher of the minimum tax or the alternative minimum tax. The credit may be carried over indefinitely or it may be refunded at the election of the taxpayer.

If the qualified agricultural property is converted to nonqualified use, no credit is allowed for the conversion year. If the conversion occurs during the two taxable years following the first year in which the credit was claimed, the total of all credits claimed must be recaptured. If land is involved and only a part of such land is converted, only a portion of the credit is recaptured. The amount which is recaptured is determined by multiplying the total of all credits claimed by a fraction the numerator of which is the number of acres of land converted to nonqualifying use and the denominator of which is the total qualifying acreage owned immediately before conversion. Involuntary conversion of agricultural property does not trigger recapture, nor does a sale of the property if qualified use is continued by the new owner.

Real property taxes paid on qualified agricultural property and deducted in determining federal taxable income must be added to federal taxable income in determining entire net income to the extent of the agricultural property tax credit allowed. (Chapter 309, Laws of 1996)

S Corporation Rate

An unintended rate increase under Article 9-A on small business S corporations for tax years beginning in 1995 has been corrected. The rate has been changed from .40625 percent to .125 percent. The rate has also been restored to .125 percent for all S corporations after 1995. Since the Tax Department processed 1995 tax returns using the .125 percent, taxpayers do not need to file an amended return or request a refund. (Chapter 309, Laws of 1996)

Savings Institutions (Thrifts)

Federal law, Public Law 104-188, enacted on August 20, 1996, repealed the bad debt deduction provided to thrift institutions by section 593 of the Internal Revenue Code (IRC) for periods beginning after December 31, 1995. Accordingly, thrift institutions will now be required for federal income tax purposes to account for their losses from loans in the same manner as commercial banks. Therefore, thrift institutions that qualify as large banks will be required to use the direct charge off method. Thrift institutions that qualify as small banks will be able to continue to use the reserve method but their allowable deduction must be computed using the experience method.

The New York State Tax Law was amended on July 30, 1996 to essentially maintain the level of deduction provided to thrifts under state law by, in general, replicating in section 1453(h) the provisions of section 593 of the IRC. Section 593 of the IRC allowed thrift institutions a bad debt deduction in computing federal taxable income which was based, in general, on the larger of the percentage of taxable income method or the experience method. Before the New York State amendment was enacted, the calculation of the New York State bad debt deduction for thrifts was tied to the deduction provided under section 593 of the IRC.

In addition the amendment provides that any amount a thrift institution is required to include in federal taxable income as a recapture of a portion of its bad debt reserve, either because of certain distributions of property to shareholders or because of the recovery of the bad debt reserve required by the aforementioned federal legislation, will not be included in entire net income.

Also provided in the legislation is an amendment to subsection (i) of section 1453 (the bad debt deduction provided to commercial banks) to clarify how an institution which has ceased to be a thrift institution establishes the starting point for its reserve for losses on loans for purposes of section 1453(i).

These provisions are applicable for taxable years beginning after 1995. (Chapter 411, Laws of 1996)