New York Commission suggests major tax overhaul

November 15, 2013

In brief

In its final report, issued on November 11, 2013, New York Governor Andrew Cuomo's Tax Reform and Fairness Commission made several recommendations to reform the state's tax provisions. Noting that "New York's taxes are still too high and its tax code too complex, placing undue burdens on individuals and business," the Commission proposed that the State: reform its corporate franchise tax and bank franchise tax, including merging the two taxes and requiring mandatory combined reporting; modernizing the sales tax; modifying the estate tax; updating local property tax administration; and simplifying tax administration. [New York State, Tax Reform and Fairness Commission, Final Report, November 2013]

On November 14, 2013, Governor Cuomo said that the report "represents another step in that direction as we seek to simplify New York's antiquated and unnecessarily onerous tax code, and to ease the tax burden on families and businesses statewide." The press release noted that this report will be shared with the state's Tax Relief Commission, which will provide recommendations for consideration in the Governor's 2014 State of the State message. [Press Release, 11/14/13]

In detail

The Commission's recommendations are presented as a menu of options, with an overall goal of revenue neutrality and an expectation that not all the recommendations will be adopted. Key suggested recommendations are summarized below.

Corporate tax reform

The Commission noted the complex nature of the state's corporate tax system: banks taxed under Article 32 of the Tax Law, and general business corporations taxed under Article 9-A; the difficulties in determining which entities are taxed under which article; the tax system includes 'disincentives' for service businesses to employ people in the state; and that more than 20 percent of tax collections are received following the completion of an audit. These corporate tax reform proposals are largely based on, but not identical to, previous state tax reform recommendations made by a working group led by the Department of Taxation and Finance (view a summary). The earlier tax reform proposals made specific recommendations, including the repeal of the exemption for income from subsidiary capital, modification of net operating loss provisions, and suggestions as to what is included in business income. The current proposal does not provide for such specificity.

The Commission recommends the following:

- merge the Bank Franchise Tax into the Corporate Franchise Tax;
- adopt a single receipts factor apportionment formula, with customer sourcing rules;

- adopt full water's-edge unitary combined filing with a 50% ownership threshold (taxpayers would have the option to make a binding sever-year election to establish composition of the group);
- adopt economic nexus standards;
- more effectively focus exemptions for subsidiary and investment income;
- eliminate certain special deductions and exemptions;
- adopt 'effectively connected' income as the starting point for the corporate tax base calculation for non-U.S. corporations;
- adopt combined reporting for all captive insurance companies;
- repeal the 'tax treaty' exception to the royalty addback provision;
- provide for the mandatory attribution of interest expenses to exempt income with expanded direct tracing of interest expense in certain situations;
- modify the alternative tax bases to create a credit for tax paid to other states to address possible constitutional challenges to these taxes;
- reform the Investment Tax Credit (limiting the credit to manufacturers of goods and eliminating the credit for used property) and the Brownfield Credit;
- repeal the Financial Services Investment Tax Credit; and
- reduce the Empire State Film Production Tax Credit allocation.

In addition, the Commission suggests that the State: take additional steps to evaluate the effectiveness of its incentive programs, streamline its corporate audit process; and accelerate the phase-out of the Temporary Utility Assessment. Lastly, the State recommends that New York City follow suit and conform with any tax reform enacted by the state.

Sales tax reform

The Commission presented its sales tax reform recommendations as a series of four independent options.

The first option calls for a repeal of the current exemption for items of clothing and footwear costing less than $110. To ameliorate the burden the repeal would create for low and middle income taxpayers, the Commission recommends enhancing the Household Credit or Earned Income Tax Credit, creating a new sales tax relief credit, or providing property tax relief.

The second option calls for the sales tax base to be expanded to digital products, such as music streaming services, electronic books, and video on demand. This option also calls for elimination of the state exemption for energy service companies, self-storage facilities, and sales through coin-operated vending machines.

Option three calls for a discussion on how to better align the sales tax base with current consumption trends and increase uniformity between the State and local tax bases. The Commission recognized the controversial nature of this option as it calls for taxing goods and services not currently subject to tax, such as personal services, admission to sporting events and performances, for example.

The last sales tax reform option calls for, if base-broadening is adopted, the creation of a tax reserve reduction fund to finance future real property tax relief and personal income tax relief.

Estate and gift tax reform

The Commission recommends:

- increasing the estate tax exemption from $1 million to $3 million (eliminating almost 75% of estates from the tax);
- eliminating the generation-skipping tax (not a major source of revenue for the state);
- reinstating the gift tax OR require estates to add back the value of any gifts above a certain threshold; and
- eliminating the 'resident trust loophole'.

Real property tax administration and tax simplification

The Commission made the following recommendations:

- establish a clear, statutory standard of assessment;
- require reassessments at periodic intervals of not less than five years;
- modify state aid programs; and
- have the state assess all complex commercial, industrial and utility property, which are currently assessed locally.

In the area of tax simplification, the Commission put forth several suggestions to make filing easier, including, but not limited to:

- replacing the requirement that a tax professional obtain a signed signature document from a client prior to transmitting a return through the Federal/State program with certification language that states that the preparer has provided a copy of the return that is being filed to the taxpayer, and

that the taxpayer has authorized the preparer to e-file it;

- establishing a 14-day in-state threshold before a nonresident would owe New York taxes;
- raising the filing threshold that triggers a requirement to file a personal income tax return;
- simplifying the filing of amended personal income tax returns;
- increasing the sales tax annual filing threshold;
- combining the MTA surcharge with the corporate tax return;
- greater cooperation, including increased joint audits, between the State and New York City; and
- repealing a series of so-called nuisance taxes that raised minimal revenue.

The takeaway

Given Governor Cuomo's stated support for tax reform, taxpayers should pay attention to the report to be issued by the Tax Relief Commission and then, his 2014 State of State address. Although there is no estimate as to when tax reform will finally come to New York, taxpayers should remain proactive when dealing with the State's current tax structure, including undertaking sales tax reviews, combined reporting analysis, examination of their apportionment methodology, and the potential qualification for the reduced tax rate on manufacturers or the investment tax credit.

Let's talk

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