New York State Department of Taxation and Finance
Office of Counsel

TSB-A-18(1)C
Corporation Tax
TSB-A-18(4)I
Income Tax
December 11, 2018

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. Z170808A

The Department of Taxation and Finance received a Petition for Advisory Opinion from [redacted] and its subsidiaries (collectively, "Petitioners"), including [redacted] ("Subsidiary"), asking: (1) whether, as a member of a unitary group making a combined report[1], Subsidiary's income from a line of business that it previously conducted, created or developed is income that must be disregarded when computing its tax factor for its Tax-free NY area ("TFA") tax elimination credit under the START-UP NY program[2]; and (2) whether proportional recovery of tax benefits in a given taxable year would preclude eligible Subsidiary employees from claiming, in that year, an exemption from the New York State personal income tax, the New York City personal income tax, the Yonkers city income tax, and the Yonkers nonresident earnings tax (collectively, the "employee income tax benefits").

We conclude that Subsidiary's income from a line of business that it previously conducted, created or developed is income that must be disregarded when computing its tax factor for its TFA tax elimination credit and Subsidiary must disregard this income even if it was received or generated outside of this State. We also conclude that Subsidiary's employees working in the TFA will continue to qualify for the employee income tax benefits if Subsidiary is subject to proportional recovery of tax benefits resulting in its suspension from participation in the START-UP NY Program if they are engaged in work performed exclusively within the TFA in net new jobs created by Subsidiary in the TFA for at least one-half of the taxable year.

Facts

Subsidiary is a registered investment manager and commodity trading advisor. The firm primarily provides its investment management services to investment companies. According to the Petition, Subsidiary is part of a worldwide financial organization with many subsidiaries and affiliates involved in similar and related lines of business. It provides investment management services to U.S.-registered investment companies focused on replicating, to the extent possible, the investment performance of various market indices for fixed income, cash management, equity and multi-assets strategies (otherwise known as exchange-traded funds or ETFs).

[1] Tax Law § 210-C.
[2] Also known as the "SUNY Tax-free Areas to Revitalize and Transform UPstate New York program." EDL § 430.

Subsidiary's operations throughout the United States are substantially focused on the creation, management and sale of ETFs. Subsidiary manages Petitioners' ETF business in the United States. Employees of Petitioners' subsidiaries and affiliates, located throughout the United States and in this State, provide investment management, technology and cash management services to Subsidiary, as well as human resources, global marketing, communications, finance and related business operations.

Subsidiary has not had any property or payroll in the State but, as part of Petitioners' unitary business, it is included in Petitioners' combined return under Tax Law Article 9-A.[3] Subsidiary was approved[4] in 2016 by Empire State Development[5] to participate in the START-UP NY program as part of an expansion of Petitioners' current operations.[6] As part of its application for the START-UP NY program, Subsidiary outlined that the jobs it would create would include data center support functions and core technology and support functions for business and corporate operations.[7]

Subsidiary has chosen proportional recovery of tax benefits as the consequence of its realizing job creation less than the amount of net new jobs it estimated in its application for the START-UP NY program.

Analysis

Issue 1

A business that is accepted into the START-UP NY program and locates in a TFA is eligible for the tax benefits specified in Tax Law § 39, including the TFA tax elimination credit.[8] Tax Law § 40 addresses the TFA tax elimination credit that, as pertinent here, allows an approved[9] business located in a TFA a credit[10] against tax under Article 9-A. According to Tax Law § 40(b), the amount of the credit is the product of the business' TFA allocation factor[11] and the business' tax factor.

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[3] From the facts in the Petition, we are assuming that, in prior years, Subsidiary was properly included in a combined return even though it may not have been a taxpayer because it had no property or payroll in the State. After 2014, taxpayers with sufficient economic nexus with the State are taxpayers in the State (see Tax Law § 209). For purposes of this Advisory Opinion, it is irrelevant whether Subsidiary is properly included in a combined return as a taxpayer or non-taxpayer.

[4] Pursuant to subparagraph iii, paragraph 1, subdivision c, section 220.6 of title 5 of the Compilation of Codes, Rules and Regulations of the State of New York [5 NYCRR 220.6(c)(1)(iii)].

[5] The chief economic development agency of the State.

[6] The Department of Taxation and Finance does not opine on Subsidiary's eligibility to participate in the START-UP NY program.

[7] The Petition indicates that the TFA would be located in the Buffalo area.

[8] EDL § 434(1).

[9] Pursuant to Article 21 of the EDL.

[10] Tax Law § 210-B(41).

[11] The percentage representing the business' economic presence in the TFA in relation to its economic presence in the State. Tax Law § 40(c).

In general, an Article 9-A business' tax factor is the largest of the amounts of tax determined for the taxable year under Tax Law § 210(1)(a), (b) or (d)[12] after the deduction of any other credits allowable under Article 9-A.[13] However, where an approved business located in a TFA is required or permitted to make a report on a combined basis under Article 9-A, such as is Subsidiary, the business' tax factor is the amount of tax determined under Tax Law § 40(d)(1) that is attributable to the income of such business.[14] This attribution is made in accordance with the ratio of the business' income allocated within the State (calculated as if such business was filing separately) to the combined group's income allocated within the State.[15] Accordingly, the amount of the TFA business' tax factor is determined by multiplying the combined group's tax amount by this ratio.[16] Pertinent here, Tax Law § 40(d)(4) provides that if a TFA business is generating or receiving income from a line of business that was previously conducted, created or developed by the business, the tax factor is adjusted to disregard such income.

As a member of Petitioners' combined group, Subsidiary's income from the ETF business, as well as its other lines of business, has been included in the computation of the combined group's business income for tax years prior to Subsidiary's acceptance into the START-UP NY program. Petitioners ask whether, as a member of a unitary group making a combined report, Subsidiary's income from a line of business that it previously conducted, created or developed and that was included in the computation of the combined group's business income is income that must be disregarded when computing Subsidiary's tax factor for its TFA tax elimination credit. Petitioners contend that this income should not be disregarded because previous income from this line of business arose from activities outside New York, arguing that requiring income from this line of business to be disregarded would provide no incentive for companies to participate in the START-UP NY program and expand their business in New York. However, the language in Tax Law § 40(d)(4) is straight-forward. There is no geographic limitation in that provision. Therefore, we conclude that Tax Law § 40(d)(4) requires Subsidiary to disregard this income when calculating its income for purposes of the ratio described in the paragraph above that is used to determine Subsidiary's tax factor for its TFA tax elimination credit under the START-UP NY program. Further, Subsidiary must disregard this income even if previous income from this line of business was received or generated outside of this State.

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[12] That is, the largest of: (1) the business' tax on its business income base or capital base, or (2) the business' fixed dollar minimum tax.
[13] Tax Law § 40(d)(1).
[14] Tax Law § 40(d)(3)(A).
[15] Tax Law § 40(d)(3)(A) and (B).
[16] The amount of tax determined under Tax Law § 40(d)(1) that is attributable to the income of a business located in a TFA may also be determined in accordance with such other methods that the Tax Commissioner may prescribe as providing an apportionment that reasonably reflects the portion of the combined group's tax attributable to the income of such business. Tax Law § 40(d)(3)(A).

Issue 2

Petitioners next ask what effect, if any, proportional recovery of tax benefits from Subsidiary, in a given taxable year, would have on the ability of Subsidiary's employees, in that taxable year, to claim the employee income tax benefits.

Subject to the limitations of EDL § 434(2), individual employees of a business that is accepted into the START-UP NY program and locates in a TFA are eligible for the employee income tax benefits provided the requirements of Tax Law § 39(e) are met. These benefits include the subtraction from federal adjusted gross income ("AGI") of any wages received by an employee of a business located within a TFA during the first five years of such business' ten-year taxable period specified in Tax Law § 39(a), to the extent included in federal AGI. During the second five years of such business' ten-year taxable period, the benefit includes the subtraction from federal AGI of the first $200,000 of such wages in the case of a taxpayer filing as a single individual, the first $250,000 of such wages in the case of a taxpayer filing as a head of household, and $300,000 of such wages in the case of a taxpayer filing a joint return, to the extent included in federal AGI.

To be eligible for the employee income tax benefits, Tax Law § 39(e) requires that the employee: (1) must be engaged in work performed exclusively at the location of such business within the TFA area during the taxable year, (2) must be engaged in work at that location within the TFA for at least one-half of the taxable year, and (3) must be employed by such business in a net new job created by such business in the TFA.

Additionally, for the employee to be eligible for the employee income tax benefits, the TFA business must satisfy the eligibility criteria specified in EDL § 433(1)(b)[17] by demonstrating that it will, in its first year of operation, create net new jobs and then, after its first year of operation, maintain net new jobs. In addition, the average number of employees of the business, and its related persons in the State, during the year must equal or exceed the sum of: (1) the average number of employees of the business and its related persons in the State during the year immediately preceding the year in which the business submits its application to locate in a TFA; and (2) net new jobs of the business in the TFA during the year. The average number of employees of the business and its related persons in the State is determined by adding together the total number of employees of the business and its related persons in the State on March 31st, June 30th, September 30th and December 31st and dividing the total by the number of such dates occurring within such year.[18]

If, at any time, the sponsoring campus, university or college, or the Commissioner of Economic Development ("Commissioner") determines that a business no longer satisfies any of the eligibility criteria specified in EDL § 433, that sponsor must recommend to the Commissioner that the Commissioner terminate, or the Commissioner on his or her own

[17] Tax Law § 39(a).
[18] EDL § 433(1)(b).

initiative must immediately terminate, such business' participation in the START-UP NY program. Upon such termination, that business will not be eligible for the tax benefits specified in Tax Law § 39 for that or any future taxable year, calendar quarter or sales tax quarter, although employees of the business may continue to claim the income tax benefits for their wages received from a business located within the TFA during the remainder of that taxable year.[19]

Further, the Commissioner must remove any business from the START-UP NY program for failing to meet any of the eligibility criteria set forth in 5 NYCRR 220.6 or any other requirement, as well as the intended purpose, of Article 21 of the EDL.[20] These criteria relate broadly to a business' eligibility to participate in the program and go beyond the business' eligibility for the program's tax benefits. Upon such removal, the business will not be eligible for the tax benefits described in Tax Law § 39 for that or any future taxable year, calendar quarter or sales tax quarter, although here, too, an employee of such business may continue to claim the income tax benefits for wages received from a business located within a TFA during the remainder of that employee's taxable year.[21]

To participate in the START-UP NY program, an eligible business must submit an application that includes a statement of performance benchmarks identifying the number of net new jobs that must be created, the schedule forecasting a five-year plan or projection for creating those jobs, and details on job titles and expected salaries.[22] A business applicant also must include a statement of consequences for its failure to meet performance benchmarks, as determined by the business applicant and the sponsor, which shall include one or more of the following: (1) suspension of such business' participation in the START-UP NY program for one or more taxable years as specified in such application; (2) termination of such business' participation in the START-UP NY program; or (3) proportional recovery of tax benefits awarded under the START-UP NY program as specified in Tax Law § 39.[23]

Under the regulations of the Commissioner, in the event the business chooses proportional recovery of tax benefits as its consequence for realizing job creation less than the estimated amount, and the number of net new jobs created is at least 75% of the number of net new jobs promised, then the tax benefits shall be reduced by the percentage by which the business failed to meet its performance benchmark, calculated as the ratio of the difference between net new jobs promised and actual net new jobs created, divided by the net new jobs promised.[24] In the event that the business chooses proportional recovery of tax benefits as its consequence for realizing job creation less than the estimated amount, and the number of net new jobs created is less than 75% of the number of net new jobs promised in any three years

[19] EDL § 436(4)(b).
[20] 5 NYCRR 220.14(c).
[21] 5 NYCRR 220.14(f).
[22] 5 NYCRR 220.10(d)(5).
[23] 5 NYCRR 220.10(d)(6).
[24] 5 NYCRR 220.10(d)(6)(a).

during the 10-year job creation schedule, then: (1) in the first year that the business does not meet 75% of its job creation benchmark, there shall be a proportional recovery of tax benefits; (2) in the second year that the business does not meet 75% of its benchmark, such business' participation in the START-UP NY program will be suspended; and (3) in the third year that the business does not meet 75% of its benchmark, such business' participation in the START-UP NY program may be terminated.[25]

As outlined above, for Subsidiary's employees to claim the employee income tax benefits, they must be engaged in work performed exclusively within the TFA, in net new jobs created by Subsidiary in the TFA, for at least one-half of the taxable year. Additionally, Subsidiary must have created or maintained those net new jobs in that taxable year while it, and its related persons, have not eliminated any other existing jobs outside of the TFA in the State. This opinion assumes that Subsidiary has created the net new jobs in which the employees in question are employed and that Subsidiary, and its related persons, have not eliminated any other jobs in the State.

Proportional recovery contemplates that a TFA business may fail to meet its performance benchmarks of realizing job creation, though it has created some net new jobs in the TFA in which are working its current employees. Upon realizing job creation less than the amount estimated by the TFA business in its program application, proportional recovery leads to suspension of the business' participation in the START-UP NY program only if the number of net new jobs created by the TFA business is less than 75% of the number of net new jobs promised in any three years during the 10-year job creation schedule and, then, only in the second such year. Further, proportional recovery leads to termination of the business' participation in the START-UP NY program only if the number of net new jobs created by the TFA business is less than 75% of the number of net new jobs promised in any three years during the 10-year job creation schedule and, then, only in the third such year.

Petitioners are inquiring about the impact to Subsidiary's employees in the TFA if Subsidiary becomes subject to proportional recovery of the tax benefits it enjoys for participating in the START-UP NY program. Proportional recovery of tax benefits affects these employees employed in net new jobs in the TFA only if it results in the suspension of Subsidiary's participation in the START-UP NY program and, then, only if such a suspension results in those employees not being engaged in work for Subsidiary in the TFA for at least one-half of the taxable year. The START-UP NY regulations contemplate that a suspended TFA business will endeavor to meet its performance benchmarks while in the period of suspension from participation in the START-UP NY program. Therefore, employees of Subsidiary may continue to qualify for the employee income tax benefits so long as all eligibility criteria for the START-UP NY business, other than job creation or maintenance, are met. If Subsidiary's participation in the program is suspended for its failure to maintain net new jobs, employees in these jobs will qualify for the employee income tax benefits as long as they are employed in these jobs for at least one-half of the taxable year. If Subsidiary's

[25] 5 NYCRR 220.10(d)(6)(b).

participation in the START-UP NY program is terminated due to three years of job creation or maintenance underperformance, or for some other qualifying reason, Subsidiary's employees may, nonetheless, claim the employee income tax benefits for their TFA-based wages during the remainder of the taxable year of such termination.

DATED: December 11, 2018

/S/
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NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion. The information provided in this document does not cover every situation and is not intended to replace the law or change its meaning.