Department of Taxation and Finance

Instructions for Form IT-638

START-UP NY Tax Elimination Credit

Tax Law – Article 1 Section 40 and Article 22 Section 606(ww)

IT-638-I

General information

For tax years beginning on or after January 1, 2014, the tax elimination credit is available to taxpayers who are approved to participate in the SUNY Tax-Free Areas to Revitalize and Transform Upstate New York (START-UP NY) Program. This program provides tax benefits to approved businesses that locate in vacant space or land of approved public and private colleges and universities, approved strategic state assets, and New York incubators affiliated with private universities or colleges that are designated as tax-free NY areas. The program is administered by Empire State Development (ESD). Approved businesses will be issued a Form DTF-74, *Certificate of Eligibility,* by the sponsoring campus, university, or college. For additional information about the START-UP NY program, visit ESD's website at *www.esd.ny.gov* and the Tax Department's website at *www.tax.ny.gov*.

The credit is equal to the product of the tax-free NY area allocation factor and the tax factor.

Any unused amount of credit for the current tax year will be treated as an overpayment of tax to be refunded or credited to next year's tax. Interest will not be paid on the overpayment.

Eligibility

A taxpayer that is a business, or an owner of a business in the case of a business taxed as a sole proprietorship, partnership (including a limited liability company (LLC) taxed as a partnership), or New York S corporation, that is subject to tax under Tax Law Article 9-A (corporation franchise tax) or Article 22 (personal income tax), is eligible for the credit if the business:

- is approved to participate in the START-UP NY program under Economic Development Law (EDL) Article 21 by ESD;
- operates in a tax-free NY area at a location approved under EDL Article 21;
- creates and maintains net new jobs as required by EDL section 433.1(b); and
- meets an annual employment test beginning with the first year of operation as required by EDL section 433.1(b).

The net new jobs requirement and annual employment test under EDL section 433.1(b) must be met by the business on the annual performance report submitted to ESD. For more information about eligibility and net new job requirements, visit ESD's website at *www.esd.ny.gov*.

Failure to meet the eligibility requirements under EDL section 433.1(b) disqualifies the business from claiming tax benefits and may result in an assessment for previous benefits claimed.

Note: A business that has successfully completed residency in a New York State incubator pursuant to Urban Development Corporation Act section 16-v is **not** required to create or maintain net new jobs as required by EDL section 433.1(b) to claim the tax benefits under the START-UP NY program. However, to qualify for the credit, the business must at least maintain the number of employees of the business in New York State as shown on their application for entry into the program. For more information on New York State incubators, see ESD's website.

An eligible taxpayer subject to tax under Article 22 may claim the credit for 10 consecutive tax years beginning with the tax year during which the business locates in a tax-free NY area using Form IT-638. Eligible taxpayers subject to tax under Article 9-A should complete Form CT-638, *START-UP NY Tax Elimination Credit.* An approved business may not claim any other tax credit allowed under the tax law other than those under section 39, with respect to its activities or employees in a tax-free NY area.

If the approved START-UP NY business is notified by ESD that it is subject to a recovery of tax benefits due to not meeting its performance benchmarks outlined in its application, the business must reduce the credit by the percentage reduction in net new jobs as set by the performance benchmarks. For more information, see Form IT-645, *Recapture of START-UP NY Tax Benefits*, and its instructions.

Who must file

File Form IT-638 if you are an individual, a beneficiary or fiduciary of an estate or trust, a partner in a partnership, or a shareholder of a New York S corporation, and you are claiming the START-UP NY tax elimination credit.

An estate or trust that distributes the income of the START-UP NY business among itself and its beneficiaries must file Form IT-638 with Form IT-205, *Fiduciary Income Tax Return,* showing each beneficiary's share of the START-UP NY business income (Schedule C).

A partnership must file Form IT-638 with Form IT-204, *Partnership Return*.

A New York S corporation does not file Form IT-638. It must file Form CT-638. If you are a shareholder of an S corporation that has made the election under Tax Law, Article 22, section 660, obtain your share of the S corporation's START-UP NY business income, three factor business allocation factor, and START-UP NY allocation factor from the S corporation and follow the instructions on this form for claiming your credit on your personal income tax return.

Penalties for fraud

If the Commissioner of Economic Development makes a final determination that an approved business participating in the START-UP NY program has acted fraudulently in connection with its participation in the program, the business will be:

- immediately terminated from the program;
- subject to criminal penalties, including but not limited to the felony crime of offering a false instrument for filing in the first degree in accordance with Penal Law section 175.35; and
- required in that year to add back to tax the total value of all the tax benefits provided under the START-UP NY program that the business and the employees of the business have received up to the date of the final determination. The amount required to be added back is reported on the business's corporation franchise tax return if the business is taxed as a corporation or is a corporate partner of a partnership. If the owner of the business is a sole proprietor, an individual partner in a partnership, or a shareholder of a New York S corporation, the amount required to be added back is reported on their personal income tax return. See Form IT-645 and its instructions for more information.

Definitions

Value of the business's real and tangible personal property means the adjusted basis of the properties for federal income tax purposes, except in the case of rented property, where the value is eight times the gross rents payable for the rental

of the property during the tax year. However, you may use fair market value when computing your property factor if you make a one-time revocable election to use fair market value in computing the property factor for purposes of the allocation factor. The election is made by using fair market values when completing Form IT-638.

Income from the partnership means partnership items of income, gain, loss, deduction, and modifications entering into your New York adjusted gross income (NYAGI).

Specific instructions

See the instructions for your tax return for the *Privacy notification* or if you need help contacting the Tax Department.

Line A – Mark an ***X*** in the appropriate box to determine the parts of this form you need to complete.

Sole proprietors: Complete lines A through D and Schedules A, D, and E.

Partnerships: Complete lines A through D and Schedule A. Provide the partners with their share of the START-UP NY business income and the partnership's allocation factor (Schedule A). The individual partners will complete their own tax factor (Schedule D) and claim the credit on their own Form IT-638.

A married couple in a business enterprise that made an IRC 761(f) election to file two federal Schedule C forms instead of a partnership return: If you file jointly, compute your credit as if you were filing one federal Schedule C for the business (enter the total of all applicable amounts from both federal Schedule C forms). Complete lines A through D and Schedules A, D, and E.

Fiduciaries of estates and trusts: Complete lines A through D and Schedules A, C, D, and E. Provide the beneficiaries with their share of the START-UP NY business income from Schedule C and the allocation factor from Schedule A. The beneficiaries will compute their own tax factor (Schedule D) and claim the credit on their own Form IT-638.

Partners in a partnership, shareholders of a New York S corporation, and beneficiaries of an estate or trust: Complete lines A through D and Schedules B, D, and E.

Note: If you are claiming a credit from more than one entity, complete a separate Form IT-638 for each entity. Complete the applicable schedules through line 19 on those additional forms. On the first Form IT-638, include the total of all line 19 amounts from the additional Form(s) IT-638 on line 20. Place the additional Form(s) IT-638 behind the first Form IT-638 that has entries on lines 20 and 21.

Line B – Enter the number from the *Certificate of Eligibility* issued to the approved START-UP NY business. Partners, shareholders, and beneficiaries should receive this information from the partnership, S corporation, or estate or trust.

Partnerships: Submit a copy of your *Certificate of Eligibility* with Form IT-638.

Line C – Enter the name of the sponsoring campus, university, or college. If you are certified by more than one sponsor, list all sponsors. Partners, shareholders, and beneficiaries should receive this information from the partnership, S corporation, or estate or trust.

Line D – You may claim the credit for 10 consecutive tax years, starting with the first tax year the approved business that was issued the *Certificate of Eligibility* locates in a tax-free NY area. Enter a number 1 through 10 identifying the tax year of the START-UP NY business tax benefit period for which you are claiming the credit on this form.

Schedule A – Allocation factor

The *tax-free NY area allocation factor* is the percentage of the business's economic presence in the tax-free NY area where the business was approved to locate under EDL Article 21. The tax-free NY area allocation factor is a percentage computed using two factors: a property factor and a wage factor. The percentage is calculated by adding the two percentages determined on lines 2 and line 4 and then dividing the result by two.

The tax-free NY area property factor is determined by dividing:

- the average value of the business's real and tangible personal property (see *Definitions*), whether owned or rented to it, in the tax-free NY area in which the business was located, during the period covered by the taxpayer's return, by
- the average value of all the business's real and tangible personal property, whether owned or rented to it, within New York State during the period covered by the taxpayer's return.

The tax-free NY area wage factor is determined by dividing:

- the total wages, salaries, and other personal service compensation paid during the tax year to employees (except general executive officers) employed at the business's location in the tax-free NY area, by
- the total wages, salaries, and other personal service compensation paid during the tax year to all of the business's employees within New York State (except general executive officers).

Note: For Article 22 purposes, references to property, wages, salaries, and other personal service compensation are deemed to be references to those items connected with the conduct of a business.

Line 1, column A – Enter the average value of real and tangible personal property, whether owned or rented, that is located within the tax-free NY area in which the business was located during the current tax year.

Line 1, column B – Enter the average value of real and tangible personal property, whether owned or rented, that is located within New York State during the current tax year.

Line 3, column A – Enter the total wages, salaries, and other personal service compensation paid during the tax year to employees (except general executive officers) employed at the business's location in the tax-free NY area.

Line 3, column B – Enter the total wages, salaries, and other personal service compensation paid during the tax year to all of the business's employees within New York State (except general executive officers).

Schedule B – Partnership, New York S corporation, and estate or trust information

Partners, New York S corporation shareholders, and beneficiaries: Enter the appropriate information for a partnership, New York S corporation, or estate or trust from which you received a share of income from a START-UP NY business. You may obtain this information from the partnership, New York S corporation, or estate or trust.

If you are claiming a credit from more than one entity, complete a separate Form IT-638 for each entity. See *Note:* under *Specific instructions* above.

Schedule C – Beneficiary's and fiduciary's share of income from a START-UP NY business

An estate or trust must complete this schedule.

Line 7 – Enter the amount of income from a START-UP NY business allocated to New York State.

If an estate or trust allocates or assigns the income from a START-UP NY business to its beneficiaries, base the division on each beneficiary's proportionate share of the income of the estate or trust. Provide your beneficiaries with their proportionate amount of the income.

Schedule D – Tax factor

The tax factor is determined by reducing the individual's tax computed under Tax Law section 601(a) through (d) for the tax year by any other allowable credits and adjusting that reduced amount by a ratio to determine the portion that is attributable to the business at its location in the tax-free NY area.

Partners, shareholders, and beneficiary's of estates and trusts that distributed the START-UP NY area income: If you belong to more than one partnership, New York S corporation, or estate or trust, complete a separate Schedule D for each entity. See *Note:* under *Specific instructions* on page 2.

Line 11 – The tax factor is computed based on your tax after the deduction of any other allowable credits. Enter the total amount of all other credits allowed against your tax.

Line 13

If the partner's, shareholder's, or beneficiary's share of income, or the business's income in the case of a sole proprietorship, is zero or a loss, the tax factor is *0*.

In all cases, if the approved business is generating or receiving income from a line of business or intangible property that was previously conducted, created, or developed by the business or a related person (as defined under EDL section 431), this income is disregarded in the computation of the tax factor.

Sole proprietors: The START-UP NY business income allocated within New York State must be determined as if the sole proprietor was a nonresident of New York State. If all of your business activity is carried on in New York State, enter the amount of income from the START-UP NY business included in your NYAGI. If you carry on business both in and out of New York State and maintain accounts clearly showing income from New York sources, enter the income from the START-UP NY business allocated to New York State. If the New York source income of the business cannot be determined from your books and records, complete Form IT-203-A, *Business Allocation Schedule*, to compute a BAP. Multiply the income from the START-UP NY business by the BAP and enter that amount on this line.

Fiduciaries of estates or trusts: Enter the amount from Schedule C, line 9.

Beneficiaries: Enter your share of the income from the START-UP NY business allocated to New York State. This information should be provided to you by the estate or trust.

Partners in a partnership: If the partnership is an approved START-UP NY business located in a tax-free NY area, enter your income from the partnership (see *Definitions*) allocated within New York State (determined as if you were a nonresident individual) and included in your NYAGI. The partnership income allocated within New York should be provided to you by the partnership on Form IT-204-IP, *New York Partner's Schedule K-1*. Enter that amount on this line.

Shareholders of a New York S corporation: If the S corporation is an approved START-UP NY business located in a tax-free NY area, multiply your pro rata share of income from the S corporation included in your NYAGI by the S corporation's business allocation factor. **Do not** include any wages paid to you by the S corporation in this amount. The S corporation's business allocation factor is computed using a three factor formula that includes property, wages, and the New York S corporation's apportionment factor. This business allocation factor is only used for the purpose of the START-UP NY tax elimination credit and should be provided to you by the New York S corporation. Enter that amount on this line.

Line 14 – Enter your NYAGI income from Form IT-201, line 33; Form IT-203, line 32; or Form IT-205, Item B. However, do not include any losses that were included in the computation of your NYAGI.

Schedule E – Computation of credit

Line 17 – Partners, shareholders, and beneficiaries of estates and trusts that distributed the START-UP NY area income: The factor to enter on this line should be provided to you by your partnership, New York S corporation, or estate or trust.

Line 20 – If you are filing more than one Form IT-638, complete the applicable schedules through line 19 on those additional forms. On the first Form IT-638, include the total of all line 19 amounts from the additional Form(s) IT-638 and complete line 21. Place the additional Form(s) IT-638 behind the first Form IT-638 that has entries on lines 20 and 21.

Line 21 – Enter the amount from this line and code ***638*** on Form IT-201-ATT, line 12; Form IT-203-ATT, line 12; or include it on Form IT-205, line 33.