New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-M-83 (3)I
Income Tax
February 4, 1983

1982 Legislation
Safe Harbor Leases

The federal Economic Recovery Tax Act of 1981 created a new safe harbor election (IRC § 168(f)(8)) that guaranties that a transaction will be treated as a lease, rather than a financing arrangement, even though the transaction would not otherwise be a lease.

Chapter 55 of the Laws of 1982 amended Article 22, with respect to the new federal safe harbor leasing rules, by adding paragraphs (23) and (24) to section 612(b) and paragraphs (24) and (25) to section 612(c). These modifications are to be made for taxable years beginning in 1982 and 1983. The effect of these modifications is to restore the lessee to the position he would have been in had he not entered into a safe harbor lease.

For federal purposes the lessor must be a Corporation (other than a Subchapter S corporation or Personal Holding Company), a partnership where all the partners are corporations, or a grantor trust where the grantor and all the beneficiaries are corporations or partnership described above. Therefore, for personal income tax purposes the section 612(b)(23) and (24) and the section 612(c)(24) and (25) modifications are only concerned with the lessee. See TSB-M-82(15)C for the treatment of lessor and lessee corporations.

Effect of Modifications on Lessee

Required Additions:

1) Any amount which the taxpayer claimed as a deduction for federal income tax purposes solely as a result of a safe harbor election, such as the deduction for rent paid to the lessor. (Section 612(b)(23))

2) Any amount which the taxpayer would have been required to include in the computation of his federal adjusted gross income had he not made a safe harbor election. Such as the gain or recapture of the accelerated cost recovery deduction on the sale or other disposition of the "leased" property. (Section 612(b)(24))

Required Subtractions:

1) Any amount which is included in the taxpayer's federal adjusted gross income solely as a result of a safe harbor election, such as interest income received from the lessor. (Section 612(c)(24)).

2) Any amount the taxpayer could have excluded from federal adjusted gross income had he not made a safe harbor election. Such as the loss on the sale or other disposition of the "leased" property. (Section 612(c)(25))

3) The amount allowable as the depreciation deduction under IRC section 167. Since New York State is not conforming to the federal accelerated cost recovery deduction for tax years beginning in 1982 and 1983 the required subtraction is for what the taxpayer would have been allowed as depreciation under IRC section 167 not the accelerated cost recovery deduction under IRC section 168. (Section 612(c)(26)). Section 612(c)(25) requires the lessee to reduce its federal adjusted gross income by the amount of deductions including the accelerated cost recovery deductions that he would have taken had he not entered into a safe harbor lease agreement. Section 612(b)(25) requires the add back of any amount of accelerated cost recovery deduction. Therefore, these two modifications with relation to the accelerated cost recovery deduction eliminate each other, leaving the lessee with a depreciation deduction (under § 167) as provided by the Section 612(c)(26) modification.

The above modifications apply to taxable years beginning in 1982 and 1983. Therefore, for taxable years beginning in 1981 and 1984 and thereafter the above modifications are not to be made as New York State will generally conform to the federal rule of IRC section 168(f)(8) as amended.

For purposes of the New York State investment credit and the research and development credit, New York State will not be conforming to the new federal safe harbor leasing rules. Section 11 and 14 of Chapter 55 of the laws of 1982 amended sections 606(a)(4) and 606(h)(4), respectively, to provide that in determining whether the taxpayer is allowed the credits, the safe harbor election is to be disregarded. This means that the lessee will be allowed the credits where it retains beneficial ownership of the property. In no cases will the lessor be allowed either the investment or research and development credits.

Section 19 of Chapter 55 of the Laws of 1982 amended section 622(b) by adding a new paragraph (6). This amendment provides that for minimum income tax purposes the federal item of tax preference for the accelerated cost recovery deduction shall be computed as if a safe harbor election was not made. This means that the lessee must include the item of tax preference in his minimum taxable income but only if there would have been a federal item of tax preference if the property was not "leased" property. This amendment is effective for taxable years beginning on or after January 1, 1982.

The Administrative Code of the City of New York, Title T, has been correspondingly amended to conform with the amendments made to Article 22 of the New York State Tax Law.

This memorandum should be used in conjunction with TSB-M-83-(2)-I.