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New York State's Tax Reform and Reduction Act of 1987
Tax Reform Technical Corrections and
New York City Tax Reduction Act of 1987

Separate Tax on Lump-Sum Distributions

The New York State Tax Reform and Reduction Act of 1987 (Chapter 28) and the Tax Reform Technical Corrections and New York City Tax Reduction Act of 1987 (Chapter 333) have amended various sections of the New York State Tax Law and the Administrative Code of the City of New York relating to the computation of the separate tax on lump-sum distributions. The new laws adopt for New York State and New York City personal income tax purposes, the 5-year averaging provision contained in the Internal Revenue Code of 1986, and the special federal transitional rules applicable to capital gains and to individuals who have reached age 50 before January 1, 1986. The changes, explained below, apply to distributions received after 1986.

Section 603 of the Tax Law (formerly Section 601-C) imposes the separate tax on the ordinary income portion of the lump-sum distribution of resident and nonresident individuals, estates, or trusts who make an election of lump-sum treatment for federal income tax purposes under Internal Revenue Code Section 402. The amount of the tax is computed under Section 624 of the Tax Law for resident individuals, estates and trusts and Section 637 of the Tax Law for nonresident individuals, estates and trusts.

Section 11-1703 of the Administrative Code of the City of New York (formerly Section 11-1701.3) imposes the separate tax on the ordinary income portion of the lump-sum distribution of resident individuals, estates and trusts of the City of New York who make an election of lump-sum treatment for federal income tax purposes under Internal Revenue Code Section 402. The amount of tax is computed under Section 11-1724 of the Administrative Code of the City of New York.

Sections 624(a) and 637(a) of the Tax Law and Section 11-1724(a) of the Administrative Code have been amended to provide for a new 5-year averaging method for computing the separate tax on the ordinary income portion of lump-sum distributions. The 5-year method replaces the 10-year method used under prior law. The amount of the separate tax under the 5-year method is equal to five times the tax computed at the New York State single individual personal income tax rates in effect for the tax year of the distribution. For purposes of determining the tax computed at the single income tax rates for the above calculation, New York taxable income is an amount equal to one-fifth of the excess of:

(1) the total taxable amount of the lump-sum distribution for the taxable year, over

(2) the minimum distribution allowance.

The minimum distribution allowance is calculated according to Section 402(e)(1)(C) of the Internal Revenue Code.

Section 624(d) of the Tax Law and Section 11-1724(d) of the Administrative Code have been amended to provide that the definitions and special rules contained in Section 402(e)(4) of the Internal Revenue Code relating to federal lump-sum distributions will apply for New York purposes. In addition, New York State and New York City will follow, except with regard to the rates of tax, the special federal transitional rules relating to capital gains and to individuals who have reached age 50 before January 1, 1986, as specified in section 1122(h)(3), (4), (5) and (6) of the federal Tax Reform Act of 1986.

If a taxpayer elects to use any of the special federal transitional provisions, the same provisions must be used for New York State and New York City purposes. The tax is to be computed using the following rates:

a) For a taxpayer who elects to use the special capital gain phase-out treatment for distributions made after 1986 but before 1992, the phased-out capital gain amount (using the federal formula) will be taxed at the New York State and New York City rates in effect for the year of the distribution.

b) For a taxpayer who reached age 50 before January 1, 1986, and elects to use the prior capital gain provisions, the tax on the capital gain portion will be computed at a flat rate of 5.4% for New York State and 1.72% for New York City.

c) For a taxpayer who reached age 50 before January 1, 1986, and elects the 10-year averaging rules, the tax on the ordinary income portion is computed using the New York State and New York City tax rate schedules in effect for taxable years beginning in 1986.