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

TSB-M-98(5)I
Income Tax
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Recent Income Tax Changes Taking Effect in 1998 or Prior Tax Years

In 1998 and in prior years, Governor George E. Pataki signed several pieces of legislation which reduce tax rates, expand tax credits and provide new and increased deductions to taxpayers. This memorandum contains brief summaries of the legislative changes affecting the New York State and New York City personal income taxes.

The following change reflects recently enacted legislation that first affects tax years prior to 1998.

Modifications for Distributions and Income Received by a Person Who Was a Victim of Nazi Persecution or Who is a Qualified Spouse or Descendant of Such Victim

For tax years beginning on and after January 1, 1995, a New York subtraction modification is allowed for distributions, to the extent the distributions are included in federal adjusted gross income, made to the taxpayer because of his or her status as a victim of Nazi persecution or as a spouse or descendant of such a victim where the spouse or descendant is in need. (**Note**: The distributions described above are general in nature, but such distributions would ordinarily be excluded from federal adjusted gross income under various Revenue Rulings and pursuant to various United States tax treaties as being in the nature of reimbursements for the deprivation of personal or civil rights.)

A New York subtraction modification will also be allowed for items of income, to the extent the items of income are included in federal adjusted gross income, that are attributable to, derived from, or in anyway related to assets which were stolen from, hidden from, or otherwise lost to a victim of Nazi persecution immediately prior to, during and immediately after World War II. This subtraction includes, but is not limited to, interest on insurance proceeds receivable by victims of Nazi persecution under policies issued by European insurance companies immediately prior to and during World War II. However, this subtraction for items of income does not apply to assets acquired with such assets, or with the proceeds from the sale of such assets. Furthermore, taxpayers are only eligible for the deduction if they are the first recipient of the income and are either a victim of Nazi persecution, or a spouse or descendent of such victim. In contrast to the provisions summarized in the previous paragraph, the spouse or descendent of such victim, who is the first recipient of such income, is not required to be “in need” to qualify to make the subtraction modification described in this paragraph.

Both of the subtraction modifications described in the two preceding paragraphs also apply to the New York City personal income tax.

(See Tax Law, sections 612(c)(35) and 612(c)(36), and the Administrative Code of the City of New York, sections 11-1712(c)(33) and 11-1712 (c)(34).)

The following changes reflect recently enacted legislation that first affects tax years beginning in 1998.

State School Tax Reduction Credit for New York City Residents

As part of the State School Tax Relief (STAR) program enacted in 1997, a refundable State School Tax Reduction Credit is provided against the New York City income tax for New York City residents and part-year residents. The credit is effective for tax years beginning in 1998 and after. If the credit exceeds the taxpayer's New York City personal income tax for the year, the excess will be refunded, without interest. Also, proration of the credit is required if the taxpayer changes resident status during the year.

The credit amounts are:

Age 65 and over. Starting in 1998, if a taxpayer has attained the age of 65 on or before the close of the tax year:

- $125, for taxpayers who are married filing jointly (if at least one spouse is 65 or older) and for surviving spouses;
- $62.50, for taxpayers who are unmarried, a head of household, or married filing separately.

Under age 65. If a taxpayer has not attained the age of 65 during or before the tax year:

- Married filing jointly (where neither spouse is 65 or older) and surviving spouses:

Tax year	*Credit amount*
1998	$ 12
1999	$ 35
2000	$ 85
after 2000	$125

- Unmarried individuals, heads of a household or married individuals filing separately:

Tax Year	*Credit amount*
1998	$ 12
1999	$ 39
2000	$ 45
after 2000	$ 62.50

(See Tax Law, section 1310(e).)

Child and Dependent Care Credit

For tax year 1998, the maximum child and dependent care credit is increased to 100% of the amount of the federal credit for taxpayers with New York adjusted gross income of $17,000 or less. The credit is gradually phased down from 100% to 20% of the amount of the federal credit for taxpayers with New York adjusted gross income between $17,000 and $30,000. The rate is 20% for taxpayers with New York adjusted gross income over $30,000.

For tax years after 1998, taxpayers with New York adjusted gross income of $35,000 or less will be allowed 100% of the federal credit. The credit is gradually phased down from 100% to 20% of the amount of federal credit for taxpayers with New York adjusted gross income between $35,000 and $50,000. The rate is 20% for taxpayers with New York adjusted gross income over $50,000.

As it was in prior years, this is a refundable credit for residents and part-year residents.

(See Tax Law, section 606(c)(1).)

Investment Tax Credit and Economic Development Zone Investment Tax Credit for the Financial Service Industry

The investment tax credit and the economic development zone investment tax credit were amended in 1998 to expand the definition of "qualified property" to include property used by the financial service industry which is placed into service on or after October 1, 1998 and before October 1, 2003.

As a result of these amendments, qualified property now includes property principally used in the ordinary course of the taxpayer's business:

- as a broker or dealer in connection with the purchase or sale of stocks, bonds, or other securities, or of commodities, or in providing lending, loan arrangement or loan origination services to customers in connection with the purchase or sale of securities;

- of providing investment advisory services for a regulated investment company (as defined in Internal Revenue Code (IRC) section 851).

A taxpayer may claim a credit for property it purchases which is used by a broker or dealer that is an affiliate of the taxpayer, providing the affiliate principally uses the property in the qualifying activities listed above. A taxpayer may also claim a credit for property it purchases and leases to a broker or dealer that is an affiliate of the taxpayer, providing the affiliate principally uses the property in the qualifying activities listed above.

The credit is not allowed unless all or substantially all of the taxpayer's employees performing the administrative and support functions resulting from or relating to the qualifying uses of the property are located in New York State.

(See Tax Law, sections 606(a) and 606(j). Similar provisions have been added to the Business Corporation Franchise Tax (Article 9-A) and the Franchise Tax on Banking Corporations (Article 32).)

Farmers' School Tax Credit

The Farmers' School Tax Credit, which was introduced in tax year 1997, has been enhanced beginning in 1998 as follows:

- To qualify for the credit for tax year 1997, at least two-thirds of the taxpayer's federal gross income must have been from farming. To qualify for tax years beginning in 1998 and thereafter, at least two-thirds of the taxpayer's *excess federal gross income* must be from farming. *Excess federal gross income* is federal gross income reduced by the sum, not to exceed $30,000, of the following items included in federal gross income: (a) wages, salaries, tips, and other employee compensation; (b) pension payments, including social security; (c) interest and dividends; and (d) those items of gross income that are includible in the computation of net earnings from self-employment for federal income tax purposes.

- For tax year 1997, the credit was phased out between $100,000 and $150,000 of New York adjusted gross income. Beginning in 1998, the phase-out is based on *modified New York adjusted gross income*, which is the taxpayer's New York adjusted gross income reduced by any principal payments on farm indebtedness. *Farm indebtedness* is debt incurred or refinanced which is secured by farm property, provided the proceeds of the loan are used for expenditures incurred in the business of farming.

- Beginning in 1998, the definition of farming is expanded to include gross income from (1) the production of maple syrup or cider, and (2) the sale of wine from a licensed farm winery, as provided for in article six of the Alcoholic Beverage Control Law; regardless of whether the income from these operations is includible in federal Schedule F, *Profit or Loss From Farming*.

- For taxable years beginning in 1998 and thereafter, the *base acreage* amount that is used to determine the amount of allowable credit has been raised to 250 acres. Under the original law, this increase would not have taken effect until tax years beginning after 1998.

(See Tax Law, section 606(n). For further information regarding this credit, see Publication 51, *Questions and Answers on New York State's Farmers' School Tax Credit*.)

Emerging Technology Investment Gain Deferral

Taxpayers are allowed to subtract from federal adjusted gross income the amount which represents the deferral of the recognition of gain on the sale of a qualified emerging technologies investment (QETI) which is (1) held for more than 36 months and (2) rolled over into the purchase of a replacement QETI within 365 days. However, the gain on the sale of the replacement QETI can be deferred if another replacement QETI is acquired within 365 days. The gain deferral applies to any QETI sold on or after March 12, 1998. Gain deferred must be added back when the replacement QETI is sold.

For purposes of this deferral, the following definitions apply:

A *qualified emerging technology company* is a company located in New York State that has total annual product sales of $10 million or less and that meets either of the following criteria: (1) its primary products or services are classified as emerging technologies; or (2) it has research and development activities in New York State and its ratio of research and development funds to net sales equals or exceeds the average ratio for all surveyed companies classified (as determined by the National Science Foundation in the most recently published results from its Survey of Industry Research and Development, or a comparable successor survey as determined by the department).

A *qualified emerging technology investment* is the investment in the stock of a corporation or an ownership interest in a partnership or limited liability company (LLC) that is a qualified emerging technology company. A QETI is also an investment in a partnership or an LLC to the extent that such partnership or LLC invests in qualified emerging technology companies. The investment must be acquired by the taxpayer as provided in Internal Revenue Code section 1202(c)(1)(B), or from a person who acquired it pursuant to this section. IRC section 1202(c)(1)(B) requires the acquisition to be at its original issue from the company, either directly from the company or through an underwriter, and in exchange for cash, services, or property (but not stock).

(See Tax Law, sections 612(u), 612(v), 612(b)(35), and 612(c)(34).)

Credit for Solar Electric Generating Equipment

For tax years beginning in 1998 and after, an individual who purchases and installs solar electric generating equipment may be allowed a credit. The amount of the credit is 25% of the lesser of:

- expenditures made for qualified solar electric generating equipment (including design, installation, and materials costs, but not including interest or other finance charges) that is placed in service in 1998 or after; or

- an amount equal to $6.00 times the number of watts included in the rated capacity of the equipment. (The $6.00 multiplier had previously been $1.50 but was raised with the 1998 legislation to $6.00.)

In either case, the credit cannot exceed $3,750. The credit is not refundable, but any unused credit amount can be carried over for five years.

Solar electric generating equipment means a manufactured photovoltaic system with a rated capacity of not more than ten kilowatts (10,000 watts) which, when installed at a residence, uses solar energy to generate electricity for use in the residence. It must be operated in accordance with applicable government and industry standards, and must also be operated in conjunction with an electric corporation's transmission and distribution facilities.

The equipment must be used in connection with the individual's principal residence and that residence must be located in New York State.

The legislation also provides (1) a proration of the credit where two or more taxpayers share a residence and (2) a requirement that government grants not includible in federal gross income be excluded when computing the amount of expenditures.

(See Tax Law, section 606(g-1).)

Credit for Employment of Persons with Disabilities

For tax years beginning in 1998 and after, a credit is available to employers who employ persons with disabilities. The credit amount per employee can be up to $2,100. If the employer is a partnership, limited liability company, New York S corporation, or an estate or trust, the credit flows through to the partners, shareholders or beneficiaries.

A taxpayer is allowed the credit for employing a qualified employee within New York State. A *qualified employee* is an employee who:

- qualifies as a *vocational rehabilitation referral* for purposes of the federal work opportunity credit (Internal Revenue Code section 51);

- has worked for the employer on a full-time basis for at least 180 days or 400 hours; and

- is certified by the New York State Education Department's Office of Vocational and Educational Services for Individuals with Disabilities (VESID), or by the New York State Office of Family Services' Commission for the Blind and Visually Handicapped (CBVH):

  (1) as a person with a disability that constitutes or results in a substantial hardship to employment; and

  (2) who has completed or is receiving services under an individualized written rehabilitation plan by VESID or by CBVH

The amount of the credit is 35% of the *eligible wages* paid to a qualified employee. When the federal work opportunity credit is in effect (as determined by Internal Revenue Code section 51(c)(4)), eligible wages for the New York credit are the first $6,000 of *qualified second-year wages*. If the federal credit is not in effect, eligible wages for the New York credit are the first $6,000 of *qualified first-year wages*. *Qualified first-year wages* are wages paid or incurred by the taxpayer during the taxable year to a qualified employee for services rendered during the one-year period beginning with the date the employee begins work for the taxpayer. *Qualified second-year wages* are wages paid or incurred by the taxpayer during the taxable year to a qualified employee for services rendered during the one-year period beginning one year after the employee begins work for the taxpayer.

This credit is not refundable, but any unused credit can be carried over for an unlimited number of years.

(See Tax Law, section 606(o). For more information see TSB-M-98-(1)I, *Credit for Employment of Persons with Disabilities.*)

Employment Incentive Credit

The employment incentive credit, previously only available to corporate taxpayers, has been extended to the personal income tax.

The credit is applicable to taxpayers (including partners of partnerships, beneficiaries of estates and trusts, and shareholders of New York S corporations) that are allowed the investment tax credit under section 606(a) of the Tax Law. The new credit is allowed for property placed in service on or after January 1, 1997. The credit requires a level of employment for the taxable year of at least 101% of the employment level in the base year. The *base year* is the year immediately prior to the year in which the investment tax credit is allowed (or in the case of a new business, the base year is the year in which the investment tax credit is allowed).

The employment incentive credit is computed as a percentage ranging from 1.5% to 2.5% of the investment credit base (the cost or other basis of the investment credit property). The applicable percentage is dependent on the degree of increase in employment during the taxable year in which the credit is claimed over that in the base year. The credit is available in each of the two years after the year in which the investment tax credit is allowed. The credit is refundable if the taxpayer qualifies as a new business and elects to have the credit in excess of tax refunded. Otherwise, any excess credit can be carried over for up to ten years.

(See Tax Law, section 606(a-1).)

Economic Development Zone Employment Incentive Credit

The economic development zone (EDZ) employment incentive credit, currently available to corporate taxpayers under the Article 9-A of the Tax Law, has been extended to the personal income tax.

The credit is applicable to taxpayers (including partners of partnerships, beneficiaries of estates and trusts, and shareholders of New York S corporations) that are allowed the EDZ investment tax credit under section 606(j) of the Tax Law. The new credit is allowed for property placed in service on or after January 1, 1997. The credit requires a level of employment for the taxable year of at least 101% of the employment level in the base year. The *base year* is the year immediately prior to the year in which the EDZ investment tax credit is allowed (or in the case of a new business, the base year is the year in which the investment tax credit is allowed).

The EDZ employment incentive credit is 30% of the EDZ investment tax credit. The credit is available in each of the three years immediately following the tax year in which the EDZ investment tax credit is allowed. For those taxed under Article 22 only, fifty percent of the excess of this credit over the taxpayer's tax is refundable if the taxpayer qualifies as a new business and elects to have that portion refunded. Otherwise, the excess credit can be carried over indefinitely.

(See Tax Law, section 606(j-1).)

Alternative Fuels Credit

Taxpayers will be allowed a credit for electric vehicles, clean-fuel vehicle property, and clean-fuel vehicle refueling property placed in service during the tax year. The alternative fuels credit is applicable to property placed in service in a tax year beginning after 1997 and before 2003.

The amount of the credit is:

- 50% of the incremental cost of a new electric vehicle registered in New York State and for which a federal credit is allowed under Internal Revenue Code section 30. The incremental cost of a new electric vehicle is the difference between the cost of the electric vehicle and the cost of a similar gasoline powered vehicle. The maximum credit is $5,000 per electric vehicle.

- 60% of the cost of new clean-fuel vehicle property which is installed in or manufactured as part of a motor vehicle registered in New York State and for which a deduction is allowed under Internal Revenue Code section 179A. The maximum credit is $5,000 per clean-fuel vehicle with a gross vehicle weight rating of 14,000 pounds or less, and $10,000 for clean-fuel vehicles with a gross vehicle weight rating of more than 14,000 pounds.

- 50% of the cost of new clean-fuel refueling property that is used more than 50% in a trade or business and located in New York State and for which a deduction is allowed under Internal Revenue Code section 179A. There is no limit on the credit for clean-fuel refueling property.

Clean-fuel means natural gas, liquefied petroleum gas, hydrogen, electricity, and any other fuel that is at least 85%, singly or in combination, methanol, ethanol, any other alcohol, or ether.

The credit is not refundable, but can be carried over for an unlimited number of years. In addition, recapture of the credit may be required if the property ceases to qualify.

(See Tax Law, sections 606(p) and 606(i)(1). For further information see TSB-M-98(4)I, *Alternative Fuel Credits.*)

College Choice Tuition Savings Program

The *College Choice Tuition Savings Program* has been enacted to provide a tax incentive for saving for post-secondary education through a combination of state and federal tax benefits. The program is administered by the Office of State Comptroller and the New York State Higher Education Services Corporation. It is designed to be a *Qualified State Tuition Program* for federal income tax purposes.

Beginning in the 1998 tax year, a person may open a special higher education savings account, called a *Tuition Savings Account*, and benefit from the new state and federal tax incentives. A person who establishes an account is the only person who can contribute to it, and is considered the account owner. The account owner can be a resident or nonresident individual. The account owner must designate a single beneficiary for each account. Each year, for purposes of computing New York adjusted gross income, an account owner can subtract from federal adjusted gross income up to $5,000 for contributions to all family tuition accounts of which he or she is the owner. For a husband and wife who are each account owners, each can subtract up to $5,000 for a maximum New York State subtraction of $10,000.

Contributions to all accounts of a designated beneficiary may not exceed $100,000. Except for this overall contribution limit, there is no limit on the amount that owners may contribute each year. (However, contributions may have federal gift tax consequences.) Because of federal law, account owners do not choose how their money is invested, program funds will be invested by the program manager. These investments will be monitored by the State Comptroller.

The investment earnings on the account are deferred for both federal and State income tax purposes while held in the account. When a qualified withdrawal is made, the investment earnings are taxable to the beneficiary for federal purposes, but are exempt for New York State purposes.

To be considered a qualified withdrawal for New York State personal income tax purposes the withdrawals must be made for purposes of paying higher education expenses. This includes the use of the funds to pay for tuition, fees, books, supplies, and equipment required for enrollment or attendance at a public or private institution of higher education. Expenses for room and board are also included for students who are enrolled at least half-time. Use of the funds is not limited to New York State schools. However, the school must be recognized and approved by the regents of the University of the State of New York or accredited by a nationally recognized accrediting agency or association.

If a nonqualified withdrawal is made from the Tuition Savings Account, the entire withdrawal will be treated as taxable income by the state, and the portion of the withdrawal attributable to investment earnings will be subject to federal income tax. In addition, the owner will be subject to a federally required penalty equal to 10 % of the investment earnings withdrawn.

The program will be managed by the Teachers Insurance and Annuity Association (TIAA). For additional information, call the programs toll free customer service line: 1-**(877)-NYSAVES (697-2837**) or visit the Program website- **www.nysaves.org**

Additional information is also on the State Comptroller's home page- **www.osc.state.ny.us** and on the Higher Education Services Corporation home page-**www.hesc.com.**

(See Tax Law, sections 612(b)(34), 612(c)(32), 612(c)(33) and 658 (d)(3).)

Taxpayer Bill of Rights Act of 1997

To ensure that taxpayers are treated fairly and without prejudice, a comprehensive and meaningful Taxpayer Bill of Rights was signed into law in 1997. The Taxpayer Bill of Rights Act of 1997 gives taxpayers additional rights and equitable relief. While most of its provisions became effective in 1997, two provisions pertaining solely or predominantly to income tax become effective in 1998:

- *Offer in compromise for spouses and ex-spouses*. As of January 1, 1998, a taxpayer who is jointly and severally liable with a spouse or former spouse on a joint tax return can make an offer in compromise of the other spouse's share of liability if:

  (A) the taxpayer wishing to make the offer is, at the time of the offer, either (1) separated from the spouse with whom he or she filed the joint return under a decree of divorce or separate maintenance, a written separation agreement, or a judicial decree of separation, or (2) is not considered married within the meaning of section 7703(B) of the Internal Revenue Code (relating to certain married individuals living apart); and

  (B) it is shown that the collection of the other spouse's share of liability from the taxpayer making the offer cannot be accomplished within a reasonable period without imposing substantial economic hardship on the taxpayer.

- *Explanation of the tax due*. Any manually issued letter of proposed deficiency, notice and demand, or notice of deficiency that (a) is issued on or after July 1, 1998, by the Tax Department, and (b) is the first letter or notice issued to the taxpayer regarding the subject matter of the letter or notice, will describe the basis for the tax due and the amount due. However, an inadequate description will not invalidate any of the letters or notices.

(See Tax Law, sections 171(eighteenth-d) and 3003. For more information see TSB-M-97(5)I, *Taxpayer Bill of Rights Act of 1997*.)

Long-Term Care Integration and Finance Act of 1997

For tax years beginning in 1998 and after, taxpayers are allowed to subtract from federal adjusted gross income a portion of the fees paid by a taxpayer who is a resident of a continuing care retirement community located within New York State that has been issued a certificate of authority to operate as such by the Commissioner of Health of the State of New York. The subtraction is for the portion of the fees that are attributable to the cost of providing long-term care benefits pursuant to a continuing care contract. The attributable portion will be determined in accordance with regulations adopted by the New York State Superintendent of Insurance. The deduction is available whether or not the taxpayer itemizes his or her deductions, and it is available in addition to the New York deduction for the payment of premiums on a long-term care insurance policy. (See the caption "Subtraction Modification for Long-Term Care Health Insurance Premiums" in TSB-M-97(3)I, *Recent Income Tax Changes Taking Effect in Tax Year 1997 or 1996.*) The deduction may not exceed the limitations set forth in section 213(d)(10) of the Internal Revenue Code for purposes of eligible long-term care premiums and are subject to annual indexing. The deduction limitations set for 1998 are:

If a taxpayer's age at the end of the tax year is:	*The deduction's limitation for 1998 is*:
40 or younger	$ 210
at least 41 but not older than 50	380
at least 51 but not older than 60	770
at least 61 but not older than 70	2,050
71 or older	2,570

If taxpayers are married and filing a joint return, and both spouses qualify, they may both get the subtraction. However, one spouse may not claim the unused part of the other spouse's subtraction.

(See Tax Law, section 612(c)(32), and the Administrative Code of the City of New York, section 11-1712(c)(32).)