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

TSB-M-98
(08)C CorporationTax
(06)I Income Tax
December 1998

Tax Credits for the Financial Services Industry

Introduction

On April 28, 1998, Governor George E. Pataki signed Chapter 56 of the Laws of 1998 into law. This Chapter, in part, amended Article 9-A (Franchise Tax on Business Corporations), Article 22 (Personal Income Tax), and Article 32 (Franchise Tax on Banking Corporations) of the New York State Tax Law, to provide new tax credits for the financial services industry. These credits are the investment tax credit, the employment incentive credit, the economic development zone investment tax credit, and the economic development zone employment incentive credit. The credits may be claimed for qualified property placed in service on or after October 1, 1998, and before October 1, 2003.

The credits are available for qualified property that is *principally used* in the ordinary course of a taxpayer's business:

(1) as a broker or dealer in connection with the *purchase or sale of stocks, bonds, 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;

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

(3) as an exchange registered as a national securities exchange within the meaning of sections 3(A)(1) and 6(A) of the Securities Exchange Act of 1934, as a board of trade as defined in section 1410(a)(1) of the Not-for-Profit Corporation Law, or as an entity that is wholly owned by and that provides automation or technical services to one or more such national securities exchanges or boards of trade. Item (3) is applicable to Article 9-A taxpayers only.

The investment tax credit is available for:

- Corporations taxable under Article 9-A;
- Banking corporations taxable under Article 32; and
- Individuals, estates, and trusts taxable under Article 22.

The employment incentive credit is available for:

- Corporations taxable under Article 9-A; and
- Individuals, estates, and trusts taxable under Article 22.

The economic development zone investment tax credit and economic development zone employment incentive credit are available for:

- Corporations taxable under Article 9-A; and
- Individuals, estates, and trusts taxable under Article 22.

Corporations and individuals described above who are partners in a partnership (including members of a limited liability company (LLC), if that LLC is treated as a partnership for federal income tax purposes), shareholders of a New York S corporation, or beneficiaries of an estate or trust are also eligible for the credits.

To claim the investment tax credit or the economic development zone investment tax credit, all or a substantial portion of the employees performing the administrative and support functions resulting from or related to the qualifying uses of the property must be located in New York State. To meet this requirement, a taxpayer must maintain a requisite number of employees performing administrative and support functions in New York State in the taxable year for which the credit is claimed. A taxpayer is presumed to maintain the requisite number of employees if the average number of employees performing these functions in New York State during the taxable year for which the credit is claimed is equal to or greater than 95 % of the average number of employees performing these functions during the 36 months immediately preceding the year for which the credit is claimed. The average number of employees must be computed on a quarterly basis. However, where quarterly employment information is not available for years prior to 1998, with respect to determining the average number of employees during the 36 months immediately preceding the year for which the credit is claimed, a taxpayer may make a reasonable determination of the average number of employees based upon information available to the taxpayer.

Employees performing administrative and support functions include all employees other than the brokers, dealers, or investment advisors engaged in the activities listed in items (1) and (2) above. Generally, any employee whose compensation for the taxable year is based more than 50 % on commissions will be presumed to be a broker, dealer, or investment advisor. However, if a taxpayer does not compensate those employees who are employed as brokers, dealers, or investment advisors on a commission basis, the taxpayer must specifically identify the employees performing those functions and must exclude those employees from the employment percentage calculation.

For purposes of the investment tax credit allowed under Article 32, only those employees employed in the department (or departments) of the banking corporation that performs the broker, dealer, or investment advisory functions listed in items (1) and (2) above, are included in determining if the taxpayer has maintained a requisite number of employees performing administrative and support functions in New York State in the taxable year for which the credit is claimed.

For purposes of the investment tax credit and the economic development zone investment tax credit allowed to a national securities exchange, board of trade or other entity described in item (3) above, the taxpayer should identify those employees who are performing the administrative and support functions resulting from or related to the activities of the securities exchange, board of trade or other entity, and calculate the employment percentage using those employees.

A taxpayer may be eligible to claim the investment tax credit or the economic development zone investment tax credit for property it purchased which is principally used by an affiliate of the taxpayer in qualifying activities. (See page 4 for the definition of *qualified property* and page 10 for the definition of *affiliate*.) In these instances, the affiliate must maintain the requisite number of employees performing administrative and support functions in New York State, as described above, in the taxable year for which the credit is claimed by the taxpayer.

The 95% employment method described above is an acceptable method of determining if a taxpayer has maintained a requisite number of employees performing the administrative and support functions in New York State in the taxable year for which the credit is claimed. A taxpayer may employ an alternate method to determine eligibility. The use of an alternate method must be demonstrated to the Tax Department as an appropriate method.

Combined filers under Articles 9-A and 32 must determine on an entity by entity basis whether the requisite number of employees performing administrative and support functions in New York State has been maintained.

Investment Tax Credit (Articles 9-A, 22, and 32)

General

The investment tax credits allowed under sections 210.12, 606(a), and 1456(i) of Articles 9-A, 22, and 32, respectively, may be claimed against the respective taxes due for the taxable year during which the qualified property is placed in service. The amount of credit is a percentage of the investment credit base. The investment credit base is the *cost* or *other basis* for federal income tax purposes, of qualified property when placed in service in New York State minus any amount of *nonqualified nonrecourse financing* attributable to the property. For purposes of Article 22, the percentage used to compute the credit is **4 % of the investment credit base**. For purposes of Articles 9-A and 32, the percentage used to compute the credit is **5 % for the first $350,000,000** of the investment credit base, and **4 % for any excess amount.** For combined filers under Articles 9-A and 32, the investment credit base is the sum of the investment credit base of each corporation included in the report.

Nonqualified nonrecourse financing is any amount for which a taxpayer is protected against loss, and, generally, any amount borrowed from a person who has an interest (other than as a creditor) in the activity in which the property is used, or from someone related to a person (other than the taxpayer) who has an interest in the activity. Nonrecourse financing is nonqualified where it is not qualified commercial financing as defined in IRC section 49(a)(1).

Qualified Property

Qualified property is tangible personal property and other tangible property, including buildings and structural components of buildings, that meet all of the following requirements.

(1) The property is acquired, constructed, reconstructed, or erected by the taxpayer between October 1, 1998, and October 1, 2003.

(2) The property is depreciable according to IRC section 167.

(3) The property has a useful life of at least four years.

(4) The property was acquired by purchase according to IRC section 179(d). A taxpayer may claim a credit for property it purchases which is used by a broker, dealer, national securities exchange, or board of trade that is an affiliate of the taxpayer, provided the affiliate principally uses the property in the qualifying activities listed in (6) below. A taxpayer may also claim a credit for property it purchases and leases to a broker, dealer, national securities exchange, board of trade, or other entity described in (6)(c) below, that is an affiliate of the taxpayer, provided the affiliate principally uses the property in the qualifying activities listed in (6) below. Any contract or agreement to lease or rent, or for a license to use the property, is considered a lease.

(5) The property is located in New York State. It is not necessary that the users of the property also be located in New York State. For example, a computer system that is placed in service in New York State would qualify for the credit, even if the brokers accessing the system are located outside the state.

(6) The property is principally used in the ordinary course of a taxpayer's business:

(a) 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;

(b) of providing investment advisory services for a regulated investment company

(as defined in IRC section 851); or

(c) as an exchange registered as a national securities exchange within the meaning of sections 3(A)(1) and 6(A) of the Securities Exchange Act of 1934, as a board of trade as defined in section 1410(a)(1) of the Not-for-Profit Corporation Law, or as an entity that is wholly owned by and that provides automation or technical services to one or more such national securities exchanges or boards of trade. Item (6)(c) is applicable to Article 9-A taxpayers only.

Banking Corporations as Dealers

For purposes of Article 32, the investment tax credit is allowed for qualified property that is principally used in a banking corporation's activities as a dealer. A banking corporation is acting as a dealer when the corporation: 1) regularly purchases securities (as defined in IRC section 475(c)(2)) or commodities (as defined in IRC section 475(e)) from or sells securities or commodities to customers in the ordinary course of its trade or business; or 2) regularly offers to enter into, assume, offset, assign or otherwise terminate positions in securities or commodities with customers in the ordinary course of its trade or business. The credit is not allowed for property located in the banking corporation's trading department unless the property is principally used by the taxpayer in the ordinary course of the taxpayer's business as a dealer. On audit, it will be the responsibility of the taxpayer to demonstrate that the qualified property for which it is claiming a credit as a dealer is, in fact, principally used in the ordinary course of the taxpayer's business as a dealer.

Application, Carryover, and Refund of Credit

Article 9-A

The investment tax credit may not reduce the tax liability for the current taxable year to less than the greater of the tax on the minimum taxable income base or the fixed dollar minimum. Any amount of credit not used in the current year may be carried forward to the next 15 taxable years.

A taxpayer which qualifies as a **new business** may elect to receive a refund instead of carrying forward the unused portion of the credit. The Tax Law does not allow for the payment of interest on the refund.

A *new business* is defined as any corporation **except**:

(a) a corporation in which more than 50% of the number of shares of stock entitling their holders to vote for the election of directors or trustees is owned or controlled, directly or indirectly, by a taxpayer subject to tax under Article 9-A; sections 183,

184, 185, or 186 of Article 9; Article 32; or Article 33 of the Tax Law;

(b) a corporation that is substantially similar in operation and in ownership to a business entity or entities taxable or previously taxable under Article 9-A; sections 183, 184, 185, or 186 of Article 9; Article 32 or Article 33 of the Tax Law; Article 23 of the Tax Law or that would have been subject to the tax under Article 23 (as that article was in effect on January 1, 1980), or the income (or losses) of which is (or was) includable under Article 22 where the intent and purpose of sections 210.12(j) and 210.12(e) of the Tax Law for refunding of credit to new business would be evaded; or

(c) a corporation that has been subject to tax under Article 9-A for more than four taxable years (excluding short periods) before the taxable year during which the taxpayer first becomes eligible for the investment tax credit.

Article 22

If the amount of investment tax credit exceeds the taxpayer's tax for the current taxable year, the amount not used in the current year may be carried forward to the next 10 taxable years.

A taxpayer which qualifies as the **owner of a new business** may elect to receive a refund instead of carrying forward the unused portion of the credit. The Tax Law does not allow for the payment of interest on the refund.

The *owner of a new business* is an individual who is either a sole proprietor or a member of a partnership **unless**:

(a) the individual has previously received a refund of an investment tax credit;

(b) the business of which the individual is an owner is substantially similar in operation and in ownership to a business entity taxable, or previously taxable under Article 9-A; sections 183, 184, 185, or 186 of Article 9; Article 32 or Article 33 of the Tax Law; Article 23 of the Tax Law or that would have been subject to the tax under Article 23 (as that article was in effect on January 1, 1980), or the income (or losses) of which is (or was) includable under Article 22 of the Tax Law where the intent and purpose of sections 606(a)(10) and 606(a)(5) of the Tax Law for refunding of credit to new business would be evaded; or

(c) the individual has operated the new business entity for more than four years prior to the first day of the taxable year during which such individual first becomes eligible for the investment tax credit.

The *owner of a new business* also includes a shareholder of a New York S corporation provided the S corporation qualifies as a *new business*. (See page 5 for the definition of *new business* under Article 9-A and see below for the definition of *new business* under Article 32.)

Article 32

The investment tax credit may not reduce the tax liability for the current taxable year to less than the fixed dollar minimum tax of $250. Any amount of credit not used in the current year may be carried forward to the next 15 taxable years.

A taxpayer which qualifies as a **new business** may elect to receive a refund instead of carrying forward the unused portion of the credit. The Tax Law does not allow for the payment of interest on the refund.

A *new business* is defined as any banking corporation **except**:

(a) a corporation in which more than 50% of the number of shares of stock entitling their holders to vote for the election of directors or trustees is owned or controlled, directly or indirectly, by a taxpayer subject to tax under Article 9-A; sections 183, 184, 185, or 186 of Article 9; Article 32 or Article 33 of the Tax Law;

(b) a corporation that is substantially similar in operation and in ownership to a business entity or entities taxable or previously taxable under Article 9-A; sections 183, 184, 185, or 186 of Article 9; Article 32; or Article 33 of the Tax Law; Article 23 of the Tax Law or that would have been subject to the tax under Article 23 (as that article was in effect on January 1, 1980), or the income (or losses) of which is (or was) includable under Article 22 where the intent and purpose of sections 1456(i)(5) and 1456(i)(8) of the Tax Law for refunding of credit to new business would be evaded; or

(c) a corporation that has been subject to tax under Article 32 for more than four taxable years (excluding short periods) prior to the taxable year during which the taxpayer first becomes eligible for the investment tax credit.

Recapture of Credit

If property on which an investment tax credit has been claimed is disposed of or ceases to be in qualified use prior to the end of its useful life, the difference between the credit taken and the credit allowed for actual use must be added back to the tax otherwise due in the year of disposition or disqualification. In addition, if at the end of a taxable year there is a net increase in nonqualified

nonrecourse financing, the decrease in the investment tax credit that results from the net increase must be recaptured.

An **additional recapture** amount equal to the original recapture amount multiplied by the interest rate on underpayments (without compounding) in effect on the last day of the taxable year must also be computed and added back to the tax otherwise due.

Employment Incentive Credit (Articles 9-A and 22)

A taxpayer that is allowed an investment tax credit under Article 9-A or 22, as described above, may also be eligible for an employment incentive credit allowed under sections 210.12-D and 606(a-1) of Articles 9-A and 22, respectively. The employment incentive credit is allowed for each of the two years immediately following the year in which the investment tax credit was allowed, provided the taxpayer's average number of employees in New York State (computed on a quarterly basis) is at least 101% of the average number of employees during the employment base year. (For purposes of Article 9-A, general executive officers are not considered employees.) The employment base year is the taxable year immediately prior to the taxable year for which the investment tax credit was allowed. If a taxpayer was not subject to tax under Article 9-A or 22, and therefore did not have a taxable year immediately prior to the taxable year for which the investment tax credit was allowed, the employment base year is the taxable year for which the investment tax credit was allowed.

The amount of the credit is a percentage of the investment credit base. Where the average number of employees during the taxable year (computed on a quarterly basis) expressed as a percentage of the average number of employees in the employment base year is at least 101% but less than 102% , the credit allowed is 1.5% of the investment credit base; where it is less than 103% but at least 102%, the credit allowed is 2% of the base; and where it is at least 103%, the credit allowed is 2.5% of the base.

The employment incentive credit allowed under Article 9-A may not reduce the tax liability for the current tax year to less than the greater of the tax on the minimum taxable income base or the fixed dollar minimum. Any amount of credit not used in the current year may be carried forward to the next 15 taxable years.

For purposes of Article 22, if the amount of the employment incentive credit allowed exceeds the taxpayer's tax for the current taxable year, the amount not used in the current year may be carried forward to the next 10 taxable years. A taxpayer which qualifies as the **owner of a new business** may elect to receive a refund of the employment incentive credit allowed under Article 22 instead of carrying forward the unused portion of the credit. (See page 6 for the definition of *owner of a new business*.) The Tax Law does not allow for the payment of interest on the refund.

A taxpayer that has claimed an investment tax credit for property it purchased which is principally used by an affiliate of the taxpayer, may also be eligible for an employment incentive credit. In this case, the credit is allowed based on the taxpayer's average number of employees in New York State. The number of the affiliate's employees is not taken into consideration.

Economic Development Zone Investment Tax Credit (Articles 9-A and 22)

The economic development zone investment tax credits allowed under sections 210.12-B and 606(j) of Articles 9-A and 22, respectively, may be claimed against the respective taxes due for the taxable year during which the qualified property is placed in service in an economic development zone in New York State. (See page 4 for the definition of *qualified property*.) A taxpayer must be certified or have applied for certification as required by Article 18-B of the General Municipal Law to claim the credit. The amount of the credit is a percentage of the cost or other basis for federal income tax purposes of qualified property when placed in service. The percentage is 10 % for the credit allowed under Article 9-A, and 8 % for the credit allowed under Article 22.

For purposes of Article 9-A, the economic development zone investment tax credit allowed may not reduce the tax liability for the current tax year to less than the greater of the tax on the minimum taxable income base or the fixed dollar minimum. Any amount of credit not used in the current year may be carried forward to the following year or years. A taxpayer which qualifies as a **new business** may elect to receive a refund of 50 % of the unused credit instead of carrying forward such amount. (See page 5 for the definition of a *new business*.)

For purposes of Article 22, if the economic development zone investment tax credit allowed exceeds the taxpayer's tax for the current taxable year, the amount not used in the current year may be carried forward to the following year or years. A taxpayer which qualifies as the **owner of a new business** may elect to receive a refund of 50 % of the unused credit instead of carrying forward such amount. (See page 6 for the definition of *owner of a new business*.)

Economic Development Zone Employment Incentive Credit (Articles 9-A and 22)

A taxpayer that is allowed an economic development zone investment tax credit under Article 9-A or 22, as described above, may also be eligible for the economic development zone employment incentive credit allowed under sections 210.12-C and 606(j-1) of Article 9-A or 22, respectively. The economic development zone employment incentive credit is allowed for each of the three years immediately following the year for which the economic development zone investment tax credit was allowed, provided the taxpayer's average number of employees (computed on a quarterly basis)

employed in the zone is at least 101% of the taxpayer's average number of employees employed in the zone during the taxable year immediately preceding the taxable year for which the economic development zone investment tax credit was allowed. (For purposes of Article 9-A, general executive officers are not considered employees.) The amount of the credit is 30 % of the economic development zone investment tax credit.

If a taxpayer was not subject to tax under Articles 9-A or 22, and therefore did not have a taxable year immediately prior to the taxable year for which the economic development investment tax credit was allowed, the taxpayer's average number of employees employed in the zone in the taxable year for which the economic development zone employment incentive tax credit is claimed must be at least 101% of the taxpayer's average number of employees in the zone during the taxable year for which the economic development zone investment tax credit was allowed.

The economic development zone employment incentive credit allowed under Article 9-A may not reduce the tax liability for the current taxable year to less than the greater of the tax on the minimum taxable income base or the fixed dollar minimum. Any amount of credit not used in the current year may be carried forward to the following year or years.

For purposes of Article 22, if the amount of economic development zone employment incentive tax credit exceeds the taxpayer's tax for the current taxable year, the amount not used in the current year may be carried forward to the following year or years. A taxpayer which qualifies as the **owner of a new business** may elect to receive a refund of 50 % of the unused credit in lieu of carrying forward such amount. (See page 6 for the definition of *owner of a new business*.) The Tax Law does not allow for the payment of interest on the refund.

A taxpayer that has claimed an economic development zone investment tax credit for property it purchased which is principally used by an affiliate of the taxpayer, may also be eligible for an economic development zone employment incentive credit. In this case, the credit is allowed based on the taxpayer's average number of employees in New York State. The number of the affiliate's employees is not taken into consideration.

Definitions

Purchase or sale of stocks, bonds, or other securities, or of commodities means, but is not limited to, issuance, entering into, assumption, offset, assignment, termination, or transfer of stocks, bonds, or other securities (as defined in IRC section 475(c)(2)), or of commodities (as defined in IRC section 475(e)).

Affiliate means:
1) a partnership 80% or more of whose interest in the partnership's capital or profits is owned

or controlled, directly or indirectly, by the taxpayer;

2) a corporation 80% or more of whose voting stock is owned or controlled, directly or indirectly, by the taxpayer;

3) a corporation who owns or controls, directly or indirectly, 80% or more of the voting stock of the taxpayer; and

4) a corporation 80% or more of whose voting stock is owned or controlled, directly or indirectly, by the entity that owns or controls, directly or indirectly, 80% or more of the voting stock of the taxpayer.

Principally used means more than 50 %. A building or an addition to a building is principally used in qualifying activities where more than 50 % of its usable business floor space is used in qualifying activities. Floor space used for bathrooms, cafeterias, and lounges is not usable business floor space. Equipment is principally used in qualifying activities when it is used in such activities more than 50 % of its operating time. Operating time may be determined based on actual time, cost allocations to individual business units, or any other reasonable method that accurately reflects operating time.

Cost means the basis of property as defined in IRC section 1012.

Other basis means the adjusted basis for determining gain or loss used as the basis for depreciation according to IRC section 167(g).