July 26, 2018

New York State Department of Taxation and Finance
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Albany, NY 12226

To Whom It May Concern:

Thank you for the opportunity to submit comments on the Bill Discussion Draft. To analyze the Tax Cuts and Jobs Act (TCJA) and identify and evaluate options for appropriate State and local government action, in December 2017 the Citizens Budget Commission (CBC) convened a Special Committee that oversaw the development of Practical Policy in Challenging Circumstances: How New York State and New York City Should Respond to the Tax Cuts and Jobs Act released on March 18, 2018. The report’s recommendations included the creation of a state business tax on pass-through entities—an Unincorporated Business Tax (UBT).

Upon reviewing the Discussion Draft Article 24-A CBC continues to support this effort to protect New York’s competitiveness for residents and businesses by blunting the impact TCJA’s $10,000 cap on a taxpayer’s deduction of state and local taxes (SALT cap).

CBC recommends:

1. **Expanding the proposed UBT to include S-corporations and sole proprietors, and conforming the UBT income apportionment formula as closely as feasible to each business organizational form’s existing formula for sourcing revenues under the personal income tax.** Expanding to these business organizational forms would provide New Yorkers greater relief from the SALT cap. For S-corporations the UBT should use the existing applicable single factor apportionment formula.

2. **Making the UBT optional by an election at the entity level.** The UBT is likely to blunt the SALT cap for most of those affected, but it may increase overall tax liability for others who do not have sufficient state income tax liability for the credit to offset, including out of state partners, residents who claim credit for tax paid to other states, those with insufficient taxable income, and partnerships exempt from tax (for example, foreign investment partners). It also would impose potentially significant compliance costs on businesses whose owners are unaffected by the SALT cap. Making the UBT optional would reduce risk to the taxpayer by providing choice.

If the State decides to proceed with a mandatory UBT, it should exempt lower net income unincorporated businesses to address circumstances when the burden and costs of filing and administration would outweigh the UBT’s
benefits. Additional analysis should inform the choice of exemption threshold. CBC’s preliminary analysis suggests that $500,000 in State taxable net income would be an appropriate level at which to impose the tax.

3. **Preserving the proposed 5 percent rate.** This rate combined with the 93 percent credit would provide significant benefit—substantially more than half of the SALT cap impact for the applicable income. A higher rate(s), either flat or in progressive net income brackets, would provide more benefits for higher income taxpayers who may choose to change their domiciles; but, it also would limit the benefit or increase liability for taxpayers who could not use the full credit. The State could revisit the rate in the future after successful initial implementation.

4. **Preserving the proposed 93 percent personal income tax credit.** This credit combined with the 5 percent rate will provide significant benefit. The State could consider modifying the credit rate in the future after successful initial implementation. The State’s goal of revenue neutrality is very important, and the State should ensure that this tax, as is or modified based on comments, does not increase State revenues. This recommendation is predicated on the UBT not being added back for taxable State income purposes, as discussed in the next recommendation.

5. **Expressly reflecting in law that the UBT is not added back for taxable State income purposes.** Current State law and the Bill Discussion Draft may require that an allocable share of the UBT be added back to an individual partner’s or member’s federal adjusted gross income to determine New York State taxable income, just as the New York City UBT is currently added back to determine New York State taxable income. Current State law and the Bill Discussion Draft should be modified to clarify that the UBT is not added back.

6. **Making the UBT credit non-refundable.** Reducing the risk of a legal challenge to the tax outweighs the benefits of making it refundable.

7. **Modifying statutory language to strengthen the case for deductibility.** Expressly stating that the UBT is a "tax imposed on the net business operations of the unincorporated business itself on account of its carrying on a trade or business" may add substantive strength to the tax’s underlying logic.

Similar changes in the New York City UBT and the Metropolitan Commuter Transportation Mobility Tax (MCTMT) statutory language should be considered. A thorough review of the language would identify opportunities for improvement.

8. **Working with other states to align tax provisions.** Since States have different apportionment rules and interstate credits, and the same income can
be taxed by multiple states, and as such, some taxpayers may be worse off than they were before the UBT. New York should work with other states, including California, New Jersey, and Connecticut, to align credits and apportionment rules in order to maximize the UBT’s benefits and minimize cases in which multiple states tax the same income or taxpayers are disadvantaged by the UBT.

We appreciate the opportunity to submit these comments and welcome any questions you may have.

Respectfully submitted,

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President