July 5, 2018

BY EMAIL (FEDERAL.TAX.RESPONSE.COMMENTS@TAX.NY.GOV)

NYS Department of Taxation and Finance
Building 9
W. A. Harriman Campus
Albany, NY 12227

Re: Discussion Draft of an Unincorporated Business Tax

Dear Ladies and Gentlemen:

We are writing on behalf of the State Tax After Reform (“STAR”) Partnership\(^1\) in response to your request for comments with respect to the discussion draft issued of a potential New York State Unincorporated Business Tax (the “State UBT”).

We understand that, in the wake of federal tax reform, New York’s desire in potentially imposing a State UBT is to “shift non-deductible individual income taxes to a deductible business tax on pass-through businesses, or some subset of pass-through businesses, and credit part or all of the value of the tax to the owners of the business on their personal income taxes.” Preliminary Report on the Federal Tax Cuts and Jobs Act, NYS Dep’t of Tax. and Fin., January 2018. p.13.

We further understand that the potential enactment of a State UBT is not intended to impose any increased financial burden on corporate taxpayers, which are still able to deduct their state income taxes at the federal level. However, despite this intent, our members are concerned that the State UBT, as currently drafted, could have a substantial negative financial impact on particular corporate partners.

**Analysis of Current Draft State UBT Provisions:** As currently drafted, the State UBT structure would provide corporate partners with a credit in the amount of the State UBT paid by the partnership that the partners can use to offset their New York State corporate franchise tax liability (the “Article 9-A Tax”). We further understand that such credit can be carried forward indefinitely.

While the availability of the credit should help mitigate the impact of the State UBT for some of our members, it should be noted that there are a substantial number of C corporations that are not subject to the Article 9-A Tax, such as utilities, insurance companies, and telecommunications companies. Thus, the credit will in no way mitigate the financial impact of the State UBT on these types of entities.

Moreover, the State UBT credit may have minimal impact even with respect to some corporate partners that are subject to the Article 9-A Tax because the tax liability imposed upon income generated by

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\(^1\) Please visit our website ([www.star-partners.org](http://www.star-partners.org)) for more information about the STAR Partnership and our work.
partnerships under the State UBT may be substantially larger than the tax liability imposed upon a corporate partner pursuant to the Article 9-A Tax. This mismatch could occur for a myriad of reasons, including if the corporate partner has losses from other sources that offset any income flowing up from the partnership. Additionally, a mismatch could be caused by the different apportionment methods that would be applied to partnerships under the State UBT and to their corporate partners under the Article 9-A Tax.

The proposed method for apportioning income for purposes of the State UBT is to use a three-factor apportionment formula comprised of a payroll factor, a property factor, and a gross income factor. This is very different from the single receipts-factor, market-based apportionment formula used to apportion the income of corporations subject to the Article 9-A Tax. The use of these very dissimilar methods could result in drastically dissimilar results with respect to the tax liability imposed on the same income; of particular concern is the fact that corporate partners in partnerships that have a large New York presence could have some of the largest variances because in such cases the partnership will have large payroll and property factors attributable to New York State.

Accordingly, while we understand that the ability to carryforward the State UBT credit is designed to offset the potential impact if a corporation cannot use a State UBT credit in a certain year, it is very possible that some corporations will never be able to use the State UBT credits, even if such credits can be carried forward indefinitely.

Due to these issues, we request that the State UBT either be made optional or that the income attributable to both direct and indirect corporate partners be carved out of the tax basis. (This second method is similar to the method used by Connecticut with respect to its newly enacted UBT, wherein pass through entities can elect to use an alternative tax base that effectively carves out the portion of tax that would be attributable to direct and indirect corporate partners.)

Please let us know if you would like to arrange an in-person or telephone meeting to discuss any of these issues in more depth.

Sincerely,

[Signature]

Joseph R. Crosby
Co-Executive Director
STAR Partnership