



BDO Seidman, LLP
Accountants and Consultants

Subject:

Changes Included in New York State's Budget

July 2007

State and Local Tax Alert

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Material discussed in this tax alert is meant to provide general information and should not be acted on without professional advice tailored to your firm's individual needs.

New York Combined Reporting

New York is moving aggressively toward combined reporting for its corporate taxpayers. Two significant developments provide taxpayers with guidance on New York's combined reporting regime. First, Governor Eliot Spitzer signed legislation that makes fundamental changes to New York's combined reporting laws. Second, the New York Department of Taxation and Finance has issued a memorandum interpreting and explaining these changes.

Combined Reporting Changes

On April 10, Governor Spitzer signed legislation that made several important amendments to the tax law. Most significantly, the legislation made a fundamental change in corporate combined reporting under the corporate franchise tax (Article 9-A). New York historically required (and permitted) combined reporting where necessary to eliminate distortion, i.e., the underreporting of New York income as a result of non-arm's-length transactions among affiliates.

Effective for tax years beginning on or after January 1, 2007, affiliated corporations that are taxable under New York's Article 9-A will be required to file combined state reports "if there are substantial intercorporate transactions among the related corporations, regardless of the transfer price for such intercorporate transactions." 2007 N.Y. S.N. 2110, Part J, amending Tax Law §211 (4)(a).

Further, the legislation provides that it is not necessary for any one corporation to have substantial transactions with every other related corporation; it is sufficient that such transactions occur "between the taxpayer and a related corporation or collectively, a group of such related corporations."

However, in situations where substantial intercorporate transactions do not exist, taxpayers or the Audit Division will still be able to argue that combination is required to cure distortion arising from the intercompany relationships.

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Guidance from the New York Department of Taxation and Finance

In response to this important change to the combined reporting law, on June 25, 2007, the New York Department of Taxation and Finance issued TSB-M-07(6)C outlining the steps corporate taxpayers should take to determine whether a combined report is required and, if so, which corporations are in the combined group. The TSB-M also provides guidance on whether the Department may require or permit taxpayers to file a combined report with one or more related corporations even where substantial intercorporate transactions are absent.

Future Guidance

Although the amendments to TSB-M-07(6)C provide some guidance on combined reporting in New York, the New York Department of Taxation and Finance has indicated that it will issue additional regulations in the future to further explain the recently revised statute.

Business Tax Rate Reductions

The new law contains several tax rate cuts. The tax cuts include a reduction in the Article 9-A rate on the entire net income base (ENI) from 7.5 percent to 7.1 percent; a reduction of the ENI rate to 6.5 percent for qualified New York manufacturers; a reduction in the Article 9-A alternative minimum taxable income rate from 2.5 percent to 1.5 percent; a reduction in the Article 32 Bank Tax ENI rate from 7.5 percent to 7.1 percent; and a reduction in the Article 33 Insurance Tax rate on life insurance company income from 7.5 percent to 7.1 percent.

Single Sales Factor Acceleration

During 2005, New York enacted legislation that amended the business allocation percentage from a three factor apportionment formula to a single receipts factor, which was to be phased-in starting in 2006. The effective date of the single receipts factor was for tax years beginning on or after January 1, 2008.

The legislation signed by the Governor on April 10, 2007 accelerated the effective date of the single receipts factor by one year, making the single receipts factor effective for tax years beginning January 1, 2007. The accelerated date of the single receipts factor will require taxpayers to change the calculation of their New York franchise tax liability for the current year. In addition, the new tax rates will require taxpayers to adjust their New York tax positions for FIN 48 purposes. Furthermore, for purposes of FAS 109, taxpayers must take into account the future New York franchise tax consequences of events that were recognized in the taxpayers' financial statements and/or tax returns.