New York State Department of Taxation and Finance
Office of Counsel
Advisory Opinion Unit

TSB-A-09(2)I
Income Tax
February 9, 2009

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. I080930B

The petition asks whether the 2006 and 2007 stock-based income of [redacted] (Petitioner) was earned by him pursuant to a non-competition agreement while a resident of Alabama and, as such, is not subject to New York income tax.

We conclude that the reinstated non-qualified restricted shares and stock option units Petitioner received for signing the non-competition agreement with Merrill Lynch are not subject to New York income tax.

Facts

Petitioner was a resident of Connecticut and an employee of Merrill Lynch in its New York City office until March 31, 2005. Petitioner submitted his resignation from Merrill Lynch on January 26, 2005. He received non-qualified restricted shares and stock option units (hereinafter RSU) in February 2004 and 2005 related to his performance for the preceding year. The RSU agreements, however, provided that all outstanding RSUs would expire and be forfeited on a date 30 days following the date of the employee's termination unless the employee was given reduction in staff status. Following the submission of his resignation, Petitioner was approached by Merrill Lynch and asked to: (1) assist Merrill Lynch in the retaining and transitioning of his primary clients; (2) continue to work for Merrill Lynch until March 31, 2005; and (3) sign a non-competition agreement which, for a period of three years, prohibited Petitioner from working at a recognized investment bank. The terms of the non-competition agreement state that, in return for signing and complying with the agreement, Merrill Lynch would reinstate his forfeited RSUs, and his resignation was given a reduction in staff status which allowed the RSUs to vest. The non-competition agreement does not include any provisions concerning compensation for Petitioner's other post resignation activities on behalf of Merrill Lynch. Petitioner, for his post resignation activities, continued to receive his regular salary, which he reported on his 2005 New York nonresident return.

Analysis

A nonresident is subject to New York personal income tax on the net amount of items of income, gain, loss, and deduction included in the nonresident's federal adjusted gross income that are derived from or connected with New York sources. (Tax Law §631(a)). Items of income, gain, loss, and deduction derived from or connected with New York sources include those items that are either attributable to a business, trade, profession or occupation carried on in New York or income from intangible personal property, but only to the extent that such income is from property that is employed in a business, trade, profession or occupation carried on in New York. (Tax Law §§631(b)(1)(B) and 631(b)(2)). Therefore, had Petitioner remained employed with Merrill Lynch or if his voluntary termination of employment with Merrill Lynch had not caused the forfeiture of the unvested RSUs (pursuant to the RSU agreement), the RSUs would have been subject to New York income tax when they vested and/or were exercised.

Income received by a nonresident as consideration for entering into a non-competition agreement is not considered to be an item of income, gain, loss or deduction that is either attributable to a business, trade, profession, or occupation carried on in New York or income from intangible personal property, that is employed in a business, trade, profession or occupation carried on in New York. In Matter of Colitti (Tax Appeals Tribunal, June 19, 2003), the Tax Appeals Tribunal found that the payment a nonresident received for signing a non-competition agreement was ordinary income to him but noted that "[t]he payment was made to petitioner for the observance of the covenant not to perform competing services without geographic restriction. Therefore, the taxpayer could only comply with the terms of the contract and be entitled to compensation pursuant to the agreement by refraining from performing services in

New York and elsewhere." In its conclusion, the Tribunal stated that "[i]f New York can tax petitioner because he might have performed services in New York but for the covenant, the petitioner is being taxed on a business, trade, profession or occupation *not* carried on in New York; clearly, a situation not embraced by Tax Law §631(b)(1)(B)." Thus, Petitioner, a New York nonresident, is not subject to New York income tax from the exercise of his reinstated RSUs, because the reinstatement of the RSUs was in consideration for entering into the non-competition agreement with Merrill Lynch and does not fall within one of the categories enumerated in either Tax Law §§631(b)(1)(B) or 631(b)(2).

DATED: February 9, 2009

/S/
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Director of Advisory Opinions
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NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.