

## **Federal Job Creation and Worker Assistance Act of 2002**

This memorandum explains how several provisions of the federal Job Creation and Worker Assistance Act of 2002 (“the Act”) may affect the computation of an individual’s New York adjusted gross income, which will affect the computation of New York State, city of New York, and city of Yonkers income taxes. The provisions included in this review are the:

- Establishment of the New York Liberty Zone<sup>1</sup> (Internal Revenue Code (IRC) section 1400L),
- Special depreciation allowance for certain property acquired after September 10, 2001, and before September 11, 2004, under new IRC section 168(k), and the special depreciation allowance for qualified New York Liberty Zone property (IRC section 1400L),
- Five-year carryback of net operating losses (NOLs) (IRC section 172),
- Limitation on using a nonaccrual experience method of accounting (IRC section 448(d)),
- Exclusion for foster care payments that applies to payments by qualified placement agencies (IRC section 131(b)),
- Adjustment in determining federal adjusted gross income for certain expenses of elementary and secondary school teachers (IRC section 62),
- Expansion of the federal Work Opportunity Tax Credit (WOTC) and the effect on New York’s Empire Zone (EZ) and Zone Equivalent Area (ZEA) wage tax credits (IRC section 1400L).

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<sup>1</sup>The Act defines the New York Liberty Zone as the area located on or south of Canal Street, East Broadway (east of its intersection with Canal Street), or Grand Street (east of its intersection with East Broadway) in the Borough of Manhattan in the city of New York. The definition of the Liberty Zone is necessary to administer several provisions of the Act, including the special depreciation allowance for qualified New York Liberty Zone property, and the expansion of the federal Work Opportunity Tax Credit (WOTC).

## **Provisions of the Act That Relate to the Computation of Federal Adjusted Gross Income**

The following five provisions of the Act relate to the computation of federal adjusted gross income. These provisions are briefly described below and are followed by an explanation of the effect of these provisions on New York State, New York City, and Yonkers income taxes.

### **Special depreciation allowance for certain property and the special depreciation allowance for qualified New York Liberty Zone property**

The Act provides, for federal income tax purposes, a:

- special depreciation allowance for certain property under new IRC section 168(k);  
or
- special depreciation allowance for qualified New York Liberty Zone property.

Both of the special depreciation allowances provided by the Act allow an additional first-year depreciation deduction equal to 30 % of the depreciable basis of qualified property. However, there are a number of important differences in the definitions of *qualifying property* under each of the special depreciation allowances. Also, the Act precludes the additional first-year special depreciation allowance for qualified New York Liberty Zone property that is eligible for the special depreciation allowance for certain property under IRC section 168(k).

The federal provisions apply to property placed in service after September 10, 2001, in tax years ending after such date.

### **Five-year carryback of net operating losses (NOLs)**

The Act temporarily extends, for federal income tax purposes, the general net operating loss (NOL) carryback period from two to five years, for certain NOLs arising in tax years ending in 2001 and 2002. It also provides for an election to disregard the five-year carryback and use the carryback period as it existed prior to the Act. The election, once made for any tax year, is irrevocable for that year.

The federal provisions apply to NOLs for tax years ending after December 31, 2000. Taxpayers are required to use the same carryback period for New York State income tax purposes as used for federal purposes.

### **Limitation on using a nonaccrual experience method of accounting**

Generally, a taxpayer using the accrual method of accounting did not accrue income related to services performed by that person that, based on experience, was expected to be uncollectible. Beginning in 2002, this rule applies only to taxpayers who perform services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, and consulting, or if a taxpayer's average annual gross receipts for the three prior tax years does not exceed \$5,000,000.

Taxpayers must use the same accounting method for New York State income tax purposes as used for federal purposes.

### **Exclusion for foster care payments that applies to payments by qualified placement agencies**

The Act amends the definition of *qualified foster care payment* and adds a definition for *qualified foster care placement agency*. Federal gross income does not include amounts received by a foster care provider during the tax year if the payments are qualified foster care payments.

The federal provisions apply to tax years beginning after December 31, 2001.

### **Adjustment in determining federal adjusted gross income for certain expenses of elementary and secondary school teachers**

An eligible educator can deduct, as an adjustment to income in computing federal adjusted gross income, up to \$250 in qualified expenses. These expenses can be deducted even if a taxpayer does not itemize deductions for federal income tax purposes.

The federal provisions apply to tax years beginning after December 31, 2001.

### **Effects of the Above Provisions on New York Income Tax**

The provisions of the federal Act (as described on pages 2 and 3 of this memorandum) will be reflected in the computation of an individual's federal adjusted gross income. The effect of this on New York State, New York City, and Yonkers income taxes is as follows:

#### **Full-year residents**

The starting point for computing an individual's New York tax is New York adjusted gross income. New York adjusted gross income is the individual's federal adjusted gross income as defined in the Internal Revenue Code (IRC) for the tax year, with modifications allowed under sections 612(b) and 612(c) of the New York State Tax Law. Sections 612(b) and 612(c) do not

contain any provisions requiring modifications, with regard to the provisions of the Act (as described on pages 2 and 3), in the computation of an individual's New York adjusted gross income.

Therefore, resident individuals who are eligible to take advantage of these provisions of the Act are also allowed the same benefit for New York State (and New York City and Yonkers, if applicable) income tax purposes.

### **New York State nonresidents**

Section 601(e) of the New York State Tax Law imposes a personal income tax on a nonresident individual on the individual's taxable income that is derived from New York sources. The tax is equal to the tax computed as if the individual were a New York State resident for the entire year, reduced by certain credits, multiplied by the income percentage.

The numerator of the fraction used to compute the income percentage is the individual's New York source income. The New York source income of a nonresident is the sum of the items of income, gain, loss, and deduction entering into federal adjusted gross income derived from or connected with New York sources and any New York addition and subtraction modifications under section 612(b) and 612(c) of the Tax Law that relate to income derived from New York sources.<sup>2</sup> The denominator of the fraction used to compute the income percentage is the nonresident's New York adjusted gross income from all sources for the entire year.

As previously stated, there are no modifications in sections 612(b) and 612(c) of the Tax Law that relate to the provisions of the federal Act as described on pages 2 and 3 of this memorandum. Accordingly, to the extent these provisions of the Act are reflected in a nonresident individual's federal adjusted gross income, they will be reflected in the computation of the individual's New York adjusted gross income from all sources for the entire year (the denominator of the income percentage) and the New York State tax as if a resident for the entire year. The provisions of the federal Act (as described on pages 2 and 3) would also be reflected in the calculation of the nonresident individual's New York source income (the numerator of the income percentage) to the extent these items are derived from or connected with New York sources.

### **New York State part-year residents**

A New York State part-year resident individual computes his or her New York State tax in the same manner as a nonresident individual. However, the New York source income of a part-year resident (the numerator of the income percentage) is the sum of the following:

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<sup>2</sup>Income derived from New York sources includes income attributable to a business, trade, profession, or occupation carried on in New York State.

1. the individual's New York adjusted gross income from all sources for the resident period, determined as if the individual's tax year for federal income tax purposes were limited to the resident period; and
2. the individual's New York adjusted gross income derived from New York sources for the nonresident period, determined as if the individual's tax year for federal income tax purposes were limited to the nonresident period; and
3. the special accruals required under section 639 of the Tax Law that relate to adjusted gross income.

Accordingly, the provisions of the Act (as described on pages 2 and 3 of this memorandum) that are reflected in the part-year resident individual's federal adjusted gross income will be reflected in the computation of the individual's New York adjusted gross income from all sources for the entire year (the denominator of the income percentage) and the New York State tax as if a resident for the entire year. These provisions of the Act would also be reflected in the calculation of the part-year resident individual's New York source income (the numerator of the income percentage) if the provision relates to the individual's resident period, and also to the extent these items are derived from or connected with New York sources during the nonresident period.

### **New York City part-year residents**

A New York City part-year resident individual is only subject to the New York City personal income tax for the period of residence. For a part-year resident, the New York City personal income tax is computed based upon all federal items of income, gain, loss, and deduction for the period of residence. Therefore, part-year resident individuals who are eligible to take advantage of the provisions of the Act (as described on pages 2 and 3 of this memorandum) are also allowed a benefit for New York City income tax purposes, to the extent the provisions of the Act relate to the individual's resident period.

### **Yonkers part-year residents**

A Yonkers part-year resident individual is subject to the Yonkers income tax surcharge for the period of residence. The Yonkers income tax surcharge for the period of residence is equal to the allocated net New York State tax, multiplied by the Yonkers income tax surcharge rate. The allocated net New York State tax is equal to the net New York State tax<sup>3</sup> for the entire year multiplied by a fraction. The numerator of the fraction is the individual's New York adjusted gross income for the period of residence. The denominator of the fraction is the

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<sup>3</sup>*Net New York State tax* is the individual's New York State tax computed as if the individual were a resident for the entire year, reduced by any New York State credits and increased by any other New York State taxes.

individual's New York adjusted gross income for the entire year. Therefore, part-year resident individuals who are eligible to take advantage of the provisions of the Act (as described on pages 2 and 3 of this memorandum) are also allowed a benefit for Yonkers income tax purposes, to the extent the provisions of the Act relate to the individual's resident period.

### **Amended Returns**

Many provisions of the Act are retroactive. Taxpayers who filed federal and New York State income tax returns before the signing of the new law must file amended federal and New York State income tax returns to take advantage of the benefits that are retroactive to tax year 2001. Generally, you must file an amended return within three years of the date the original return was filed, or within two years of the date the tax was paid, whichever is later. For information on filing an amended New York State personal income tax return, see the instructions for Form IT-201-X, *Amended Resident Income Tax Return*, or Form IT-203-X, *Amended Nonresident and Part-Year Resident Income Tax Return*.

### **Other Provisions of the Act**

#### **Expansion of the federal Work Opportunity Tax Credit (WOTC) and the effect on New York's Empire Zone (EZ) and Zone Equivalent Area (ZEA) wage tax credits**

The Act expands the WOTC to treat New York Liberty Zone business employees as members of a targeted group for purposes of section 51 of the IRC. In addition, the WOTC, which was scheduled to expire on December 31, 2001, was extended by the Act for two years, through December 31, 2003.

As defined in the Act, a *New York Liberty Zone business* means any trade or business located in the New York Liberty Zone, or relocated elsewhere in New York City from the New York Liberty Zone, as a result of the physical destruction or damage of such place of business by the September 11, 2001, terrorist attack. A trade or business is not a New York Liberty Zone business for any tax year in which such trade or business employed an average of more than 200 employees on business days during the tax year.

A *New York Liberty Zone business employee* means, with respect to any period, an employee of a New York Liberty Zone business if substantially all the services performed by the employee for the business during the period are performed in the New York Liberty Zone. In general, in the case of a qualified New York Liberty Zone business that is located in New York City but outside of the New York Liberty Zone, an employee is considered a New York Liberty Zone business employee if substantially all of the services performed during the period by the employee for the business are performed in New York City.

The federal provisions apply to tax years ending after December 31, 2001, and before January 1, 2004.

Although there is no corresponding New York WOTC, the expansion of the federal WOTC may affect the computation of the New York EZ and ZEA wage tax credits. New York Liberty Zone business employees, as added by the Act and defined in new section 1400L of the IRC, **may** be considered targeted employees for the purposes of the EZ and ZEA wage tax credits for tax years ending on or after January 1, 2001 (see below for additional requirements for targeted status).

To claim either the EZ or the ZEA wage tax credits, the employer must be certified under Article 18-B of the General Municipal Law and must meet certain eligibility requirements, including an employment test.

A qualified employer may treat New York Liberty Zone employees as targeted employees for the EZ and ZEA wage tax credits if all of the following conditions are met:

- the employee is a resident of New York State; and
- the employee received EZ or ZEA wages during the period for which the credit is being claimed; and
- the employee was a member of a federal targeted group at the time of initial employment in the job for which the EZ or ZEA wage tax credit is being claimed.

If the employee is considered a targeted employee for the purposes of computing the EZ or ZEA wage tax credit, the employer may be entitled to the maximum credit of \$3,000 for the employee.

For more information on these credits, see the instructions for Form IT-601, *Claim for EZ Wage Tax Credit*, and Form IT-601.1, *Claim for ZEA Wage Tax Credit*.