

New York State Tax Treatment of Connecticut  
Capital Gains, Dividends and Interest Tax

The Tax Department has recently received several inquiries as to whether the Connecticut Capital Gains, Dividends and Interest Tax constitutes an "income tax" for New York State Personal Income Tax purposes.

Section 607(a) of the New York State Tax Law provides that any term used in Article 22 shall have the same meaning as when used in a comparable text in the Internal Revenue Code, unless a different meaning is clearly required. Section 164(a) of the Internal Revenue Code allows a deduction for: "State and local, and foreign, income..., taxes." In determining what constitutes an "income tax" under section 164(a)(3) of the Code, the Federal courts agree that such a tax must be a "net income tax"; that is, a direct tax on gain or profits, and that gain is a necessary ingredient of income. See Stratton's Independence, Ltd. v Howbert, 231 US 399, 415; Eisner v Macomber, 252 US 189, 207; and Bank of America National T. & S. Assoc. v U.S., 459 F.2d 513, 517-8. In addition, the United States Tax Court, in McGowan v Commissioner, 67 T.C. 599, 610 recently stated: "A 'tax' is an 'income tax' even though it is restricted to various forms of income."

Review of the provisions of the Capital *Gains*, Dividends and Interest Tax imposed by section 12-506 of the Connecticut General Statutes shows that the tax is imposed upon the "net gain or income" of the individual taxpayer. In addition, the Internal Revenue Service, in a private letter ruling dated December 13, 1983, (LTR 8411079), held that a state capital gains and dividends tax similar to the Connecticut tax in question qualifies as a state income tax under section 164(a)(3) of the Code. Therefore, the Connecticut Capital Gains, Dividends and Interest Tax constitutes an income tax for federal and New York State income tax purposes.

Accordingly, this tax must be added back to arrive at New York State adjusted gross income to the extent that it was deducted in arriving at federal adjusted gross income (Section 612(b)(3) of the Tax Law), and the amount included as federal itemized deductions must be subtracted out in determining the New York itemized deduction (Section 615(c)(1) of the Tax Law).

In addition, New York State residents who are subject to this tax may be entitled to a resident credit, provided the tax is imposed upon income or gain from real or tangible personal property located in Connecticut, or on income from intangible personal property employed in a business, trade, profession, or occupation carried on in Connecticut. (See Part 121 of the Personal Income Tax Regulations for limitations on this credit.)

This policy is effective immediately.