

**Investment Tax Credit (ITC) Relief for Property Destroyed as a Direct Result of the Terrorist Attacks of September 11, 2001 (Articles 9-A, 22, 32, and 33)**

If property on which an investment tax credit (ITC) has been allowed is disposed of or ceases to be in qualified use prior to the end of its useful life, the difference between the original credit allowed and the credit allowed for actual use must generally be recaptured and added to the tax due in the year of disposition or disqualification. The recapture amount is augmented with interest computed at a rate equal to the underpayment rate in effect on the last day of the tax year in which the recapture occurs. Additionally, the investment credit base used in computing the ITC for any replacement property is the cost or other federal basis of the replacement property. Such cost or other federal basis, in the instance of an involuntary conversion, includes any basis reduction required by Internal Revenue Code (IRC) section 1033.

**Articles 9-A (Franchise Tax on Business Corporations), 22 (Personal Income Tax) and 32 (Franchise Tax on Banking Corporations)**

The Tax Law has been amended to provide taxpayers with an election by which they choose either to defer the required recapture for *all* qualifying property destroyed as a direct result of the terrorist attacks of September 11, 2001, or not to make the basis reduction required by the IRC for property that replaces the destroyed property. The elections are explained below.

- Taxpayers may elect to defer the amount to be recaptured for all qualifying property to the taxable year next succeeding the recapture event taxable year. The recapture event taxable year is the taxable year in which the destruction or cessation of qualified use occurred. The amount to be recaptured is computed pursuant to the recapture provisions of the Tax Law. However, if this election is made, the recapture amount must be augmented with interest computed at a rate equal to two times the underpayment rate in effect on the last day of the tax year in which the recapture occurs. Further, a taxpayer making this election that meets an employment test (explained on page 3) in the taxable year next succeeding the recapture event taxable year is not required to recapture any ITC for the qualifying property. Also, if 50% or more of a taxpayer's employees died as a direct result of the attacks, the taxpayer may elect to utilize this provision and will not be required to recapture any ITC for the qualifying property, whether or not it meets the employment test.
- In lieu of the election to defer the recapture of the ITC, a taxpayer that acquires replacement property that is similar or related in service or use to the property destroyed as a direct result of the attacks may elect to compute the investment credit base of the replacement property without regard to any basis reduction required by

IRC section 1033.<sup>1</sup> For purposes of this election, it does not matter when the destroyed property was placed in service, or whether an ITC was claimed on the destroyed property. For example, qualified property placed in service by a corporation in the financial services industry in September of 1998 that was destroyed as a direct result of the attacks, and for which an ITC was not claimed because the ITC for the financial services industry was not yet effective, may qualify for the increased investment credit base for the replacement property under this election. For those taxpayers making this election that had property destroyed for which an ITC *was* previously claimed, recapture is required in the recapture event taxable year pursuant to the provisions of Tax Law section(s) 210.12(g) and 606(a)(7).

### **How to make the election**

The election is made when the return for the recapture event taxable year is filed, by including or not including the recapture on that return. In addition, taxpayers must attach a statement to the return indicating that they have either made the election to defer recapture to the taxable year next succeeding the recapture event taxable year, or to compute the investment credit base of the replacement property without regard to any basis reduction required by IRC section 1033.

If the tax return for the recapture event taxable year has already been filed and the recapture reported on that return, it is presumed that the taxpayer has made the election to compute the investment credit base of the replacement property without regard to any basis reduction required by IRC section 1033, unless the taxpayer subsequently files an amended return to change that election.

### **Special Rule for Estates, Trusts, Partnerships, LLC's and New York S Corporations**

The election to either defer recapture or to compute the investment credit base of the replacement property without regard to any basis reduction required by IRC section 1033 is made by the estate, trust, partnership, LLC that has elected to be treated as a partnership, or New York S corporation, that owned the destroyed property. The entity making the election must notify each beneficiary, partner, member or shareholder of the election. Beneficiaries, partners, members, or shareholders are bound by the election of the entity and must include the results of that election on their tax return. Both the entity and the beneficiaries, partners, members, or shareholders must attach a statement to their returns indicating which election was applied in the preparation of the return. If an estate, trust, partnership, LLC, or New York S corporation amends its return to change

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<sup>1</sup>The term "property which is similar or related in service or use" is derived from its use in IRC section 1033. Therefore, the term will be interpreted by the Department of Taxation and Finance in such a way as to be consistent with its interpretation for federal purposes.

the election, the respective beneficiaries, partners, members, or shareholders must amend their tax returns to reflect the change of election.

### **Amended Returns**

Taxpayers may subsequently change their election by amending their previous filing and attaching a statement to the amended return indicating that they are electing on the amended return to either defer recapture to the taxable year next succeeding the recapture event taxable year, or compute the investment credit base of the replacement property without regard to any basis reduction required by IRC section 1033.

- Personal income tax filers (including partnerships, estates, and trusts) that have already filed a return for the recapture event taxable year, but wish to change their election, must complete Form IT-212, *Investment Credit* or IT-252, *Investment Tax Credit for the Financial Services Industry*, and file an amended return, including the required statement regarding the election, on Form IT-201-X, *Amended Resident Income Tax Return*; Form IT-203-X, *Amended Nonresident and Part-Year Resident Income Tax Return*; Form IT-204, *Partnership Return*; or Form IT-205, *Fiduciary Income Tax Return*.
- Corporations (including New York S corporations) that have already filed a return for the recapture event taxable year, but wish to change their election must complete Form CT-44, *Claim for Investment Tax Credit for the Financial Services Industry*, or Form CT-46, *Claim for Investment Tax Credit*, and file the appropriate amended return, including the required statement regarding the election. For information regarding the filing of amended returns, see the instructions for the return type originally filed or Form CT-8, *Claim for Credit or Refund of Corporation Tax Paid*.

### **Employment test**

The employment test applies to taxpayers that elect to defer the recapture of the ITC to the taxable year next succeeding the recapture event taxable year. Those taxpayers who meet the employment test in the succeeding year are not required to recapture any ITC for property that was destroyed or ceased to be in qualified use as a direct result of the terrorist attacks of September 11, 2001. The employment test for LLC's that have elected to be treated as partnerships, estates, trusts, partnerships, and S corporations is determined at the entity level, not by each member, beneficiary, partner or shareholder.

To meet the employment test, the taxpayer's total employment number in New York State on the last day of the taxable year next succeeding the recapture event taxable year must be a significant percentage of the taxpayer's average total employment number in New York State for the taxpayer's recapture event taxable year and the two taxable years immediately preceding the recapture event taxable year. The Department of Taxation and Finance is interpreting "significant percentage" to mean at least 75%. The taxpayer's total employment number for the employment

test includes all employees, including general executive officers, of the taxpayer employed full-time by the taxpayer in New York State.

The average total employment number for the recapture event taxable year, and the two taxable years immediately preceding the recapture event taxable year, are computed by adding the taxpayer's total employment number on March 31, June 30, September 30, and December 31 during the applicable taxable years and dividing the result by the number of those dates occurring within the applicable taxable years. However, in the case of the taxable year which includes September 11, 2001, the average total employment number for the taxable year is determined by substituting September 1, 2001, for September 30, 2001. If the taxable year included December 31, 2001, the total employment number is computed by excluding the total employment number on December 31, 2001.

### Employment test example

For tax year 2001, a calendar-year taxpayer required to recapture the ITC previously allowed for property destroyed as a direct result of the terrorist attacks on September 11, 2001, elects to defer the amount to be recaptured for **all** qualifying property to the tax return for 2002.

The taxpayer's total employment number in New York State on December 31, 2002, which is the last day of the taxable year next succeeding the recapture event taxable year, is 166. For tax year 2002, the taxpayer completes the following employment test to determine if the eligibility requirements for cancelling the recapture have been met:

	Year	March 31	June 30	Sept 30	Dec 31	Total
Total employment number in NYS	1999	205	210	210	215	840
Total employment number in NYS	2000	215	220	220	225	880
Total employment number in NYS	2001	225	225	240*	Do not include	690
Three year total						2,410

\*For 2001, the total employment number in the state on September 1, 2001, must be used in lieu of the total employment number in the state on September 30, 2001.

The average total employment number in New York State for the recapture event taxable year and the two taxable years immediately preceding the recapture event taxable year is calculated by dividing 2,410 (the three year total employment number in the state) by 11 (the total number of dates in the three-year period). In this example, the average total employment number in New York State is 219, when rounded.

To qualify to cancel the recapture, the total employment number in New York State on the last day of the taxable year next succeeding the recapture event taxable year must be at least 75% of the average total employment number in the state for the recapture event taxable year and the two taxable years immediately preceding the recapture event taxable year. Therefore, in this example, the total employment number in the state on the last day of the of the 2002 tax year must be at least 164 (calculated by multiplying 219 by 75%). Since the total employment number in New York State on December 31, 2002, is 166, the taxpayer is eligible to cancel the recapture on the 2002 tax return.

### **Article 33 (Franchise Tax on Insurance Corporations)**

An ITC was added to Article 33, by Chapter 63 of the Laws of 2000, for qualified property used by insurance corporations in providing certain financial services. The credit is available for qualified property placed in service on or after January 1, 2002, and before October 1, 2008. Although the ITC was not available to insurance corporations for property placed in service prior to January 1, 2002, an insurance corporation that acquires qualifying replacement property that is similar or related in service or use to the property destroyed as a direct result of the attacks may compute the investment credit base of the replacement property without regard to any basis reduction required by IRC section 1033. The corporation must attach a statement to the return for the tax period in which the initial ITC claim for the replacement property is made indicating that it has elected to compute the investment credit base of the replacement property without regard to any basis reduction required by IRC section 1033.

(See Tax Law sections 210.12, 606(a), 1456(i) and 1511(q)).