



New York State Tax Treatment of Nonqualified Deferred Compensation

Federal Public Law 110-343 (the “Public Law”) added § 457A to the Internal Revenue Code (IRC) to address the taxation of certain nonqualified deferred compensation attributable to services performed on or after January 1, 2009. For nonqualified deferred compensation to which IRC § 457A does not apply due solely to the fact that the amount deferred is attributable to services performed before January 1, 2009, the Public Law, Division C, § 801(d)(2) requires such deferrals, to the extent such amounts are not includable in gross income in a tax year beginning before January 1, 2018, to be included in gross income for federal tax purposes in the later of:

- the last tax year beginning before January 1, 2018; or
- the tax year in which there is no substantial risk of forfeiture of the rights to such compensation.

This memorandum addresses the New York State tax treatment of such amounts, and applies to:

- resident and nonresident individuals;
- sole proprietorships;
- partnerships (including limited liability companies [LLCs] and limited liability partnerships [LLPs] that are treated as partnerships for federal income tax purposes);
- estates and trusts; and
- Article 9-A taxpayers.

Article 22 resident individuals

Under Tax Law § 611, the New York taxable income of a resident individual is the individual’s New York adjusted gross income (NYAGI) less the individual’s New York deductions and exemptions. The NYAGI of a resident individual is the individual’s federal adjusted gross income (FAGI), taking into account any addition or subtraction modifications required under Tax Law § 612. For New York State income tax purposes, all nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) that is required to be included in FAGI in a tax year in accordance with the Public Law, Division C, § 801(d)(2), must be included in NYAGI in that tax year, if the taxpayer is a New York resident in such year.

Resident taxpayers may be allowed a resident tax credit for any income sourced to and taxed by another state. See [Form IT-112-R](#), *New York State Resident Credit*, for more information about this credit.

Article 22 nonresident individuals

Under Tax Law § 601(e), nonresident individuals are subject to tax on taxable income derived from New York sources. The New York source income of a nonresident individual is the sum of the net amount of income, gain, loss, and deductions included in the individual's FAGI and derived from or connected with New York sources, taking into account any addition or subtraction modifications required under Tax Law § 612. New York source income includes income that is included in the nonresident individual's FAGI and is related to a business, trade, profession, or occupation previously carried on in the state, whether or not as an employee. See Tax Law § 631(b)(1)(F). This income includes nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) that is required to be included in FAGI in a tax year in accordance with the Public Law, Division C, § 801(d)(2), if such compensation is related to a business, trade, profession, or occupation previously carried on in the state, whether or not as an employee.

The amount of such nonqualified deferred compensation that must be included in a nonresident's New York source income is determined as follows:

- If the business, trade, profession, or occupation was carried on wholly in New York State in the tax year the services were performed, the entire amount of nonqualified deferred compensation must be included in New York source income.
- If the business, trade, profession, or occupation was carried on wholly outside New York State in the tax year the services were performed, none of the nonqualified deferred compensation is included in New York source income.
- If the business, trade, profession, or occupation was carried on partly in and partly outside New York State during the tax year the services were performed, the amount of nonqualified deferred compensation to be included in New York source income is determined using the rules described below for:
 - an *employee*, if the nonresident performed the services as an employee; or
 - a *business*, if the nonresident was carrying on a business in New York State. For purposes of this memorandum, a *business* includes sole proprietorships and partnerships (including LLCs and LLPs that are treated as partnerships for federal income tax purposes). For the allocation rules for income earned as a nonresident shareholder of a New York S corporation, see *Taxation under Article 9-A* below.

Services previously performed partly in and partly outside New York State

Employee

If a nonresident individual is required to include nonqualified deferred compensation in FAGI in a tax year in accordance with the Public Law, Division C, § 801(d)(2), and such compensation relates to services performed as an employee in a previous tax year, the following method is used to determine the amount of such compensation that must be included in New York source income in the year such income is included in FAGI.

The individual computes a fraction:

- the numerator is the number of working days employed in New York during the tax year the services were performed; and
- the denominator is the total number of working days employed both in and outside New York during the tax year the services were performed.

Such fraction is multiplied by the amount of nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) included in FAGI that relates to services performed as an employee in that tax year. See 20 NYCRR § 132.18.

If nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) from services performed in more than one tax year is included in FAGI, these rules are applied separately for each tax year that such services were performed, and the aggregate amount of New York source income is reported on the individual's New York State nonresident income tax return for the tax year the taxpayer is required to include such nonqualified deferred compensation in FAGI for federal tax purposes.

For an employee who is a nonresident for the tax year the nonqualified deferred compensation is included in FAGI for federal tax purposes, but who was a resident for the tax year the services were performed, the amount that is included in New York source income is calculated using the same methodology described above. Taxpayers must maintain documentation to substantiate the allocation.

Business

If a nonresident individual is required for federal income tax purposes to include in FAGI any nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) that:

- is related to services performed by the nonresident individual in a previous tax year as a sole proprietor; or
- is related to services performed by a partnership (including LLCs and LLPs that are treated as partnerships for federal income tax purposes) in a previous tax year,

then the nonresident individual's New York source income related to such nonqualified deferred compensation is determined using one of the following methods:

- If the books and records of the sole proprietorship or partnership, from the year the services were provided, adequately disclose and represent the proportion of the net amount of the items of income, gain, loss and deduction derived from or connected with New York sources, the total amount of items and net amount of such items for the tax year the services were provided may be used to determine the allocation. A partnership must report these amounts to the nonresident partner on Form IT-204-IP and must also complete item P on Form IT-204-IP.

- If the books and records of the sole proprietorship or partnership, from the year the services were performed, do not adequately disclose and represent the proportion of the net amount of the items of income, gain, loss and deduction derived from or connected with New York sources, the proportion of income that is attributable to New York sources is determined using the three factor formula described in 20 NYCRR 132.15(c), calculated by the sole proprietorship or partnership for the tax year the services were performed. A partnership must report these amounts to the nonresident partner on Form IT-204-IP and must also complete item P on Form IT-204-IP.

If the methods described above do not fairly and equitably allocate and apportion the items of income, gain, loss and deduction attributable to the partnership for a tax year, the department may prescribe an alternative method of allocation. A sole proprietor or partnership may also submit an alternative method of allocation, provided that the proposed method is thoroughly explained and disclosed on the taxpayer's income tax return. If the department approves the proposed allocation and apportionment, the method may be used in lieu of the methods described above. See 20 NYCRR 132.25.

If nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) from services performed by a sole proprietor or a partnership in more than one previous tax year is included in a nonresident individual's FAGI, these rules are applied separately for each tax year that such services were performed. The aggregate amount of New York source income must be reported by a partnership to the nonresident partner, and must be reported on the nonresident individual's New York State nonresident income tax return, for the tax year the taxpayer is required to include such nonqualified deferred compensation in FAGI for federal tax purposes.

Part-year residents

If an individual changes resident status during the tax year, the rules described in this memorandum under *Article 22 resident individuals* apply where the nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) is properly reportable in the resident period of the tax year, and the rules described under *Article 22 nonresident individuals* apply where the nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) is properly reportable in the nonresident period of the tax year.

Nonresident and part-year resident estates and trusts

The rules described in this memorandum apply to nonresident estates and trusts and part-year resident trusts where the nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) is includible in the federal income of the estate or trust.

Yonkers nonresident earnings tax

The Yonkers nonresident earnings tax is imposed on wages and net earnings on self-employment attributable to a business, trade, profession, or occupation carried on in the city of Yonkers. Under the rules described in this memorandum, if an individual performed services in the city of Yonkers, the nonqualified deferred compensation (including all appreciation and

earnings related to such deferrals) is allocated to Yonkers using the same rules that apply to nonresidents of New York State.

Taxation under Article 9-A

For corporations taxable under Tax Law Article 9-A (including New York S corporations), nonqualified deferred compensation (including any appreciation and earnings related to such deferrals) that is includible in federal taxable income in accordance with the Public Law, Division C, § 801(d)(2), is considered business income under Article 9-A and is included in the apportionment factor under the rules in Tax Law § 210-A and the applicable regulations.

For a resident individual who is a shareholder of a New York S corporation, such individual's distributive share of nonqualified deferred compensation (including all appreciation and earnings related to such deferrals) from the S corporation that is required to be included in FAGI in a tax year in accordance with the Public Law, Division C, § 801(d)(2), must be included in NYAGI in that tax year.

A nonresident individual who is a shareholder of a New York S corporation determines the amount of such nonqualified deferred compensation derived from New York sources by applying the S corporation's business apportionment factor to such amounts included in New York adjusted gross income (see [TSB-M-15\(7\)C, \(6\)I](#), *Impact of New York State Corporate Tax Reform on New York S Corporations and their Nonresident and Part-Year Resident Shareholders*).

However, if a nonresident individual who is a shareholder of a New York S corporation is required to include nonqualified deferred compensation in FAGI in a tax year in accordance with the Public Law, Division C, § 801(d)(2), and such compensation relates to services performed as an employee of the S corporation in a previous tax year, then the individual must instead use the method for employees to determine the amount of nonqualified deferred compensation related to that past employment that must be included in New York source income (see *Employee* on page 2).

Note: A TSB-M is an informational statement of existing department policies or of changes to the law, regulations, or department policies. It is accurate on the date issued. Subsequent changes in the law or regulations, judicial decisions, Tax Appeals Tribunal decisions, or changes in department policies could affect the validity of the information presented in a TSB-M.