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Legal Update

Current New York Tax Considerations for Asset Managers—Part 1, Sourcing Fee Income in a Remote Work Model

Asset managers face a complicated tax environment in New York. They must consider not just New York State (NYS) business taxes on their management companies, their funds and themselves, but also parallel New York City (NYC) business taxes. Sometimes these NYS and NYC taxes are aligned, and sometimes they are not. In the case of remote work, they are not. As we discuss below, remote work presents an opportunity to reduce the New York tax burden on fee income, but NYS and NYC each present their own considerations, which must both be addressed to properly capitalize on it.

The pandemic forced many of us into a work-from-home experiment that had no precedent or road map. Many companies then learned that working from home is not only possible but, in some cases, quite efficient. As a result, after leaving NYC in March of 2020, many principals and investment professionals have decided they may stay put and never truly return to their NYC offices. Some will work from home and occasionally visit the NYC office, while others will simply establish new offices closer to their primary residence.

This Legal Update reviews key NYC Unincorporated Business Tax (UBT) and NYS Personal Income Tax (PIT) considerations—and potential savings—that may arise from this shift. It focuses on income sourcing concepts for partnerships under the UBT and PIT. The sourcing regimes largely apply to management fee income, as the UBT and PIT both have exemptions for self-trading income that shelter carried interest income from tax, when structured properly. Based on their current approaches to income sourcing, the UBT automatically adjusts to remote work locations and the PIT does not. NYS's newly enacted "Pass-Through Entity Tax" mirrors the PIT. We have discussed the Pass-Through Entity Tax in a recent Legal Update. The PIT discussion in this Legal Update applies primarily to nonresident partners because resident partners are taxable on all of their income wherever earned.

Part 2 of this Legal Update will address the PIT considerations that residents and nonresidents face at the individual level, including some basics around residency changes, and the effects of those changes on PIT liabilities. It will consider issues such as sourcing carried interest income, bonuses and deferred payments in years that involve residency changes, and establishing bona fide home offices.

I. Some Basics

A. UBT

The UBT is a 4% tax on net income that is allocated and apportioned to NYC. It applies to a base that is generally derived from federal gross income and deductions, but has its own definition of a taxable business—which notably excludes some financial and real estate investment activities—and applies its own modifications to income.[1] The result is a tax that conforms to many aspects of Subchapter K and the Internal Revenue Code, but also has its very own concepts, construction and application.

One mostly thinks of partnerships and limited liability companies in relation to the UBT, but the tax also applies to sole proprietors, trusts, and any other form of unincorporated business.[2] Whatever the form of business, determining how much income the business earned in NYC is often the most crucial determination. Many UBT filers do business inside and outside NYC and therefore must "allocate" that income to NYC to calculate the tax (most other state and local income taxes use the term "apportion" for income that is attributed by formula and the term "allocate" for income that is attributed by source).[3] NYC allocates income by using a formula that results in a "business allocation percentage" that represents the percentage of income a taxpayer must attribute to NYC in any particular year for tax purposes.

Until recently, the NYC allocation formula included three factors—property, payroll, and gross income.[4] Beginning in 2018, however, the property and payroll factors no longer apply and the NYC business allocation percentage is derived entirely from the gross income factor.[5] That means a business determines its NYC income solely by reference to the percentage of its gross receipts or sales that are attributable to NYC under the UBT's rules for sourcing gross income. For a services business, such as asset management or law or accounting services, the place of performance generally controls that determination because the gross income factor sources fees for most services to NYC to the extent the services were performed within NYC.[6] Special industry-specific rules provide a customer-based approach for registered broker-dealers and mutual fund managers[7] and those exceptions are not addressed by this Legal Update. Further flexibility may exist with respect to "other business receipts" or "other reasonable method[s]," which we have covered, in part, in this prior article.

B. PIT

The PIT is a graduated personal net income tax on residents and nonresidents at the NYS level, and on residents at the NYC level. Remote working has a greater potential impact on nonresidents than residents (except to the extent a person changes their residency as a result of remote work). This is because remote work may affect the amount of both NYS sourced business income (i.e., Form K-1 income) and NYS sourced compensation (i.e., Form W2 income) that nonresidents must report.

In contrast to the UBT, the PIT is more closely tied to federal tax returns, at least for residents. It applies to federal adjusted gross income with certain state-specific modifications.[8] That means NYS and NYC tax all of a resident's income wherever earned on almost the same basis as the federal government, subject to NYS credits for taxes paid to other state and local jurisdictions.

The analysis is a little more complicated for nonresidents. NYC does not tax nonresidents at all (which is a policy choice that solidifies the UBT's importance in NYC's tax structure), and NYS taxes nonresidents only on income earned within NYS.[9] Similar to the UBT, the PIT has complicated rules that go into determining how much income is taxable in NYS.

For business income from a partnership or sole proprietorship, the PIT apportions income with a three factor apportionment formula—property, payroll and gross income—with exceptions for directly allocated income, such as real estate rents and gains.[10] The payroll factor represents the percentage of payroll in NYS; the property factor represents the percentage of real property and tangible personal property owned or leased in NYS; and the gross income factor represents the percentage of gross income sourced to NYS. For purposes of the gross income factor, payments for services are generally sourced to NYS if the services were performed out of an office in NYS.[11] Unlike the UBT, the PIT does not have special rules for registered broker-dealers or mutual fund managers. While the PIT's gross income factor seems similar to its UBT cousin, it actually applies differently and can lead to surprisingly different results in a work-from-home circumstance.

For employee compensation, a formula based on NYS work days applies, and encompasses items such as deferred compensation or income accrued prior to changing residence.[12] That formula has been under pressure during the pandemic because it requires employees of a NYS office to treat every work day as a "NYS work day" unless he or she is working outside NYS out of "necessity."[13] We will address the considerations applicable to compensation in Part 2 of this Legal Update.

II. Remote Working Implications for Income Allocation and Apportionment

A. UBT: PERFORMANCE GENERALLY OCCURS AT A PERSON'S PHYSICAL LOCATION

i. The Legal Landscape

Management Fees. The Administrative Code states that "charges for services performed shall be allocated to the city to the extent that the services are performed within the city;" it does not go on to explain how to determine when services are performed within NYC, and the regulations are similarly silent.[14] Does an entity attribute its services to the location of its office where the services are centered, or to the location of its employees that are carrying out the service, or some combination? As explained below, the UBT's history, the NYC General Corporation Tax (GCT) regulations, and recent case law demonstrate that the business would generally look to their employees' (and contractors') locations to determine where the services are performed under the standard "place of performance" analysis.

Over the course of three years, from July 1, 2005 through July 1, 2008, the UBT phased-in a shift to this sourcing method for services under the gross income factor. Previously, the gross income factor sourced payments to the office out of which services were performed—the same method the PIT currently applies to charges for services.[15] The UBT changed to the current place of performance standard in order to conform with the sourcing provisions that applied under the GCT (those same standards still apply under the GCT, but since 2015, the GCT now only applies to S corporations; C corporations use a market-based method under the newly enacted NYC Business Corporation Tax).

A legislative summary addressing 2005 law changes in NYS and NYC states: "[i]n calculating the receipts factor of the business allocation formula, receipts from the performance of services will be allocated to the City to the extent that the services are performed in the City. (This rule replaces the one that allocates service receipts based on the location of the office out of which the employee performing the services works.)" This shift is important because it shows that NYC departed from a method under which an office location would itself determine the source of charges for services. Now, instead, the location where the services are actually being performed determines the sourcing for those charges.[16]

NYC has not, as yet, updated its regulations to reflect this change to the gross income method. That means NYC's exact approach to determining the place of performance is, at first glance, ambiguous. However, NYC specifically adopted the place of performance standard in order to conform the UBT to the GCT, and has virtually locked itself into the methods articulated in the GCT regulations and related case law. This may be the reason NYC has never updated its regulations—it may consider the GCT regulations to apply by default, though it has appeared to resist the GCT regulations on other issues. Whatever NYC's current thinking, the statutory structure and intent of the UBT's place of performance standard set a presumption that it will apply consistently with the GCT regulations and case law.

In this regard, the GCT regulations provide that taxpayers may determine the place of performance for a lump sum—i.e., a sum that compensates for activities within and without NYC—"on the basis of the relative values of, or amounts of time spent in performance of, such services within and without New York City, or by some other reasonable method."[17] The NYC audit division often uses relative values to determine place of performance, in effect applying a costs of performance method, which can include a range of expenses, or simply focus on compensation paid to specific employees and independent contractors.[18] However, the time spent and other reasonable methods are equally allowable under NYC statutes and regulations. Time spent means the hours physically worked by individual staff and contractors within and without NYC.[19] "Some other reasonable" method is a facts-and-circumstances analysis but otherwise remains undefined.[20] We have argued that some other reasonable method could include a market-based methodology, though we do not expect NYC will always agree.

A recent opinion from the NYS Appellate Division in the *Matter of Gerson Lehrman Group, Inc*. sheds light on the place of performance rule.[21] The Appellate Division affirmed the NYC Tax Appeals Tribunal, which had concluded that the locations of both independent contractors and certain employees factor into the place of performance analysis. It used the location of those individuals to attribute those costs within and without NYC. NYC had objected to including the amounts paid to the independent contractors, and the Tribunal had rejected that contention because they generated revenue for the taxpayer, who was a principal, not an agent. The opinion does not describe the details of the taxpayer's location data, but its contractors could work from virtually any location and the decision clearly indicates those locations would be taken into account. Those contractors did not need a purposeful or assigned location in order for their location to count in the receipts factor. The NYS Appellate Division had also affirmed the NYC Tax Appeals Tribunal's decision that credit rating revenues should be sourced to the locations of credit rating employees using the place of performance standard.[22]

Matter of Gerson Lehrman is also instructive for identifying the staff and contractors who may be considered in the analysis. In particular, the Court included Gerson's sales and IT staff, and consultant "managers," over the taxpayer's objection, because it felt they contributed to the overall delivery of the service. In other words, those staff members did not generate the actual information that the customers received but they contributed to providing that information to the customers. We can expect that NYC will cite this decision as authority for including support staff in place of performance calculations in some circumstances. Many businesses may focus on front office staff in their place of performance analyses, and this decision highlights that NYC will consider support staff as includible when their work is integrally related to the overall product or service. If that position is apply evenhandedly, that approach has the potential to benefit firms with a back office outside NYC, but to disadvantage firms with a back office in NYC.

Carried Interest. Because most managers that operate in NYC have segregated their carried interests into separate, passive holding companies, carried interest income often qualifies for exemption under the UBT's "self-trading" exemption.[23] Those managers that have not structured their carried interests in this manner may still seek to qualify for the "partial" self-trading exemption, which has a complicated asset-based test that is not the subject of this report. Carry that does not qualify for exemption is likely to be treated as investment incomethat is allocated to NYC using a formula that attempts to approximate the NYC presence of the businesses behind the investments, rather than the presence of the taxpayer itself. Under either scenario, remote work by the management company is not likely to materially affect UBT paid on carry. It remains to be seen, however, whether changes at the federal, state or local level will result in carry being characterized as compensation or apportionable business income. In that case, remote work locations would likely have an impact on the taxation of carry under the UBT.

ii. Potential Taxpayer and Tax Department Approaches to Remote Work under the Place of Performance Standard

For asset managers, this place of performance standard should allow considerable flexibility in allocating management fee income under the UBT (and GCT). The possibilities include sourcing gross income in proportion to:

- **the hours** that partners, front office staff, and investment professionals—or all staff that contribute to the investment management services—work within and without NYC;
- **the amounts** it paid to individuals working within and without NYC—either front office staff and investment professionals or a larger universe of employees—based on their daily location; or
- **the capital** being actively managed from locations within and without NYC on a daily, monthly, or quarterly basis, using the location of the individuals overseeing that capital or investing that capital.

While NYC and NYS have been litigating the extent to which asset managers may claim the benefit of special market-based sourcing rules that apply to registered broker-dealers, the activities of registered broker-dealers and asset managers often overlap. Some managers might reach the conclusion that their activities are sufficiently similar to a registered broker-dealer that customer sourcing is "some other reasonable method." NYC will almost certainly disagree.

Given the choice between relative value, time spent, or some other reasonable method, asset managers should have flexibility to arrive at a place of performance determination that reflects the realities of their work place. The current remote work environment undoubtedly factors into the amount of income earned in NYC. The management companies should be prepared, however, to defend their selections of staff to include in the place of performance analysis. For example, managers that rely heavily on electronic trading programs should expect NYC to evaluate the inclusion and exclusion of IT employees from their gross income factor computations.

In this regard, the management company should review its investment management and investment advisory agreements to identify the specific tasks that the funds pay it to handle. Of course, the value of each function in those agreements will differ—as investment decisions should be more valuable than administrative tasks—but the manger should compare each task to its staff performing them and select individuals to include on that basis. NYC will certainly want to make sure that the manager includes staff relevant to each task performed in NYC, whether that is appropriate or not.

However taxpayers construct their place of performance analyses, NYC would now be hard pressed to assert while COVID-19 office precautions are in place that compensation or work hours must be attributed to the offices where the taxpayers' employees and contractors worked prior to the COVID-19 pandemic. NYC shifted away from a statutory method that would have achieved just that result in favor of the place of performance method, which it has rigorously pursued through a location-based approach under which it sources gross income from services in accordance with the physical location of the people performing those services. The place of performance method should, therefore, automatically adjust to the location of partners, staff, and contractors, whether that analysis relies on costs of performance, time spent, or some other reasonable method.

NYC can nevertheless be expected to try and push income back into its tax base. To do so, it might:

- assert its discretion to adjust an apportionment method and ignore temporary work-from home-locations on the basis that they purportedly create distortion;
- assert, in conflict with the statute's history, that only fixed or assigned locations can be taken into account under the gross income factor because free floating work locations do not accurately represent where taxpayers' are earning their revenue;
- assert that the cost of an employee is attributed to his or her office, not a daily location that is within the employee's control;
- assert that the primary work location throughout the year is the best indicator for place of performance (though that approach might not achieve the result that NYC wants for 2020);
- take variations in revenue (or profitability) into account throughout the year, to try and attribute more income to the periods in which employees were at their offices, or to decrease the income attributed to periods when employees were working from home; or
- seek to include or exclude staff or costs to overweight NYC in the gross income percentage.

NYC could also attempt to change the law or promulgate new regulations, which depart from the GCT. Though, it would be tough for NYC to enact a new sourcing regime that does not shift to a market-based method after its recent changes for C corporations.

iii. Steps Taxpayers Should Take to Support Place of Performance Determinations

Any business that seeks to adapt its apportionment method to the new location of its employees will have to support that shift with documentation. NYC will certainly not accept work-from-home locations on faith; it will want to see that hours or compensation attributed to locations outside NYC are based on work actually performed outside NYC. Without adequate documentation, it will simply attribute the services of NYC-assigned employees to the business's office in NYC.

To document these new work locations, businesses should, among other things: consider updating their systems to have staff (and principals) report their actual work location; implement enterprise-level software that tracks employee locations; instruct personnel to keep their calendars up to date to reflect their work location, including calls and video conferences that will be joined from home and assignments that take place outside the office; and have personnel communicate in writing to their human resources departments, supervisors, and colleagues where they have been and will be working, with specific day counts if possible.

Smartphone apps are available to track daily whereabouts, and may show where a person was/is working when implemented by the business itself. Even then, an app's data may need to be paired with workplace documentation, like calendar entries, emails, timesheets, card swipes etc. to satisfy NYC in a tax audit. Withholding and personal income tax considerations may arise in tandem with this documentation, but, as explained below, the NYS PIT and UBT diverge in their approach to working from home.

While adjustments to NYC income allocations for 2020 and 2021 may have an immediate benefit, longer-term changes to work locations may have a more significant impact. Many key personnel will not return to the NYC office, and others will only return to the office for a fraction of their pre-pandemic hours. These more permanent changes will have an effect on UBT income allocations, but they need to be documented as well. Accordingly, businesses that expect a longer term shift to significant remote operations, or even new offices, should begin to organize formal policies and procedures that adapt the workplace to the new environment. We suggest considering:

- separate entities for separate offices inside and outside NYC, consistent with a plan for operations inside and outside NYC;
- requirements and schedules for reporting to the office in NYC;
- policies for assignment to a work-from-home location;
- standards for professional conduct, including availability, at home;
- information security standards and procedures at home;
- reimbursement for home office expenses related to the business;
- standards for hardware and technology at home, and policies and procedures for installing workplace hardware at home;
- methods and procedures for communication with staff and third parties while at home;
- updated procedures for documenting work and work time at home;
- policies for managing staff, as well as handling recruitment and on-boarding;
- updated procedures for board meetings, committee meetings, and check-ins with departments and direct reports; and
- updated procedures for investor meetings and communications if applicable.

Separate entities for separate offices can help localize income inside and outside of NYC under the UBT, though companies should expect NYC to evaluate whether a business purpose exists for disaggregating a business into separate entities for separate geographic locations. This approach may benefit from both transfer pricing studies, to attribute and document shares of fee income among related entities conducting related services, and a plan for business inside and outside NYS. The UBT does not have a combined reporting regime, which means that assigning highly-paid investment professionals to offices outside NYC under a new entity can have a meaningful impact on income allocated to NYC.

Further, with concrete policies and procedures for the remote work environment in place, the business can demonstrate its owners and staff are working from home pursuant to a mandate from the business on a basis and platform that carries out the goals of the business with purpose and intent. These kinds of steps can further establish the remote locations of staff as work locations—and places of performance. The new procedures would also likely lead to sufficient data collection to make an accurate income allocation possible.

B. PIT: RESIDENCY AND ASSIGNED OFFICE REMAIN PARAMOUNT

The NYS PIT must be considered in terms of residents and nonresidents.[24] Residents should be concerned with evaluating whether their residency has changed, and, if not, the extent to which they may credit tax paid to other states.[25] Nonresidents should be concerned with determining the amount of flow-through income that is apportioned to NYS and compensation that they themselves earned from days worked in NYS.[26] This installment of our Legal Update addresses flow-through income, and the next installment will address personal compensation allocated by work-days, as well as residency and other issues. Similar to the UBT, sourcing considerations apply almost entirely to management fee income because the PIT also has an exemption for self-trading exemption that applies to carried interest income.

i. Legal Landscape for Nonresident Partners with Respect to Flow-Through Income

Management Fees. Partnerships that earn management fee income (or any other compensatory income), and have nonresident partners, must apportion that income within and without NYS in order for their nonresident partners to determine their total NYS source income subject to tax. That means nonresident owners of partnerships and LLCs taxed as partnerships generally determine the amount of their flow-through fee income that is attributable to NYS under the PIT's rules for sourcing business income. The statute does not provide a sourcing or apportionment method and instead punts that determination to regulations. With respect to partnerships, the regulations clarify that taxpayers should use their books and records to directly allocate income, but, if the books do not fairly reflect the allocation of income, a three-factor apportionment formula applies. That formula equally weighs payroll, property, and gross income factors.[27] For companies that do business within and without NYS, in most circumstances, the books and records method does not work because income is earned from the collective efforts of multiple offices and is therefore not directly allocable to any single office.

For purposes of determining whether a work-from-home location affects the amount of PIT due, the payroll and gross income factors are the most important, and reveal that office locations will generally drive the business's income apportionment within and without NYS. The property factor is a fairly straightforward representation of real estate and tangible property owned or rented in NYS, and would not be greatly affected by remote work locations unless the business reduces its physical space in NYS as a result.

The payroll factor represents the total percentage of wages, salaries, and other personal service compensation paid to employees in connection with business carried on within NYS. The regulations are not precise regarding what compensation is paid for services in connection with operations carried on in NYS.[28] Instructions to relevant tax forms, however, provide that "compensation paid for services is in connection with operations carried on in New York State if the employee works in or travels out of an office or other place of business located in New York State."[29] Therefore, NYS generally considers the employee's office to control the payroll factor.

The gross income factor represents the percentage of receipts sourced to NYS.[30] For this purpose, payments for services are generally sourced to NYS if the services were performed from an office in NYS.[31] Payments for services of a particular employee would generally be sourced to NYS if the employee is assigned to an NYS office.[32] The statute, case law, regulations, and guidance do not describe how the gross income factor should apply in the case of a lump sum payment for services of multiple individuals. Given this uncertainty, partnerships should have some flexibility. It may be possible to divide a single revenue stream in proportion to salaries attributable to each office (as a proxy for charges for services of those employees) or of a more select group of individuals that operate as revenue generators. It is even more unclear whether the services performed by employees of affiliated entities should be included in the gross income factor, especially when the affiliated entity is compensated by an intercompany payment and it files its own return. Because the PIT does not have a combined filing regime, it would seem that intercompany payments should not factor into the analysis.

The PIT, therefore, diverges from the UBT in two critical respects: it applies a three-factor formula and it turns on the office out of which services are performed, rather than the place of performance.

How does a business determine the office out of which services are performed? The role of a business's office can be seen, ironically, through a UBT decision that applied the former NYS Unincorporated Business Tax method for sourcing gross income from services. In *Matter of Zaretsky*,[33] an orthopedic surgeon maintained an office in NYC, where he spent about 20 hours per week, as well as an office in his New Jersey residence, where he spent about 30 to 40 hours per week. He earned most of his income from serving as an expert witness and testified that he conducted most of his analysis at home. However, virtually all of the taxpayer's services were negotiated or consummated from his NYC office and he used his NYC office for his primary contact information. He also used his office to examine the subjects of his expert opinions from time to time, as well as to see the occasional patient. On his business returns, the taxpayer allocated half of his income to NYC and half of his income to New Jersey, contending that his New Jersey home office constituted a regular place of business.

Because essentially all of the taxpayer's business was negotiated and consummated from his NYC office, the former hearings bureau allocated 100% of the business gross income to NYC. The sales or charges allocated to NYC included all his sales under the statutory standard, in the Department of Finance's opinion. Under the statute, NYC gross income included all sales negotiated or consummated and charges for services performed by an individual chiefly situated at, connected by contract or otherwise with, or sent from, offices of the unincorporated business, or other agencies, situated within NYC—mirroring the standard in the PIT. In the case of this taxpayer, the Department of Finance determined his services were most chiefly connected to the NYC office and not his New Jersey home office because NYC was the hub for generating the work that led to the income.

Carried Interest. The PIT approach to income from investment activities is more flexible than the UBT approach. For reasons, that are not the subject of this Legal Update, under current NYS policy and law, it is not necessary to segregate carried interests into separate passive holding companies in order to obtain the PIT self-trading exemption for carry. That exemption allows nonresidents to exclude income from intangible property, like securities, from NYS source income, unless that property is employed in a NYS business.[34] It is always possible that NYS might assert, at some point in the future, that carried interests are employed in a NYS business. It is also possible that the proposed NYS Senate Bill S.B. 999 or a successor could pass that attempts to impose a separate fee on income from a carried interest—though the existing proposal does not apply effectively to structures where the carry is segregated into a separate passive holding company. In the event a more effective bill comes to pass, carry might be subject to a similar analysis as management fee income for sourcing purposes.

ii. Options for Partnerships with Nonresident Partners

Now, as individuals are conducting their daily responsibilities outside of NYS, what is the impact on PIT apportionment factors for management fee income? If NYS has its way, very little.

NYS's approach to the payroll factor seems fairly inflexible and would attribute salaries and bonuses to office locations, largely ignoring remote work locations unless the employer changes the employee's office assignment to a non-NYS office or a "bona fide" home office, as will be explained in Part 2 of this Legal Update (to preview, a bona fide home office has a rigid, formal standard that would be hard to satisfy in most circumstances).

NYS has similarly keyed the gross income factor to office locations, which means that factor also does not automatically take remote work locations into account, under NYS's approach. This is in contrast to the UBT's place of performance standard and, therefore, appears to offer significantly less opportunity to adjust NYS sourced income for the pandemic and remote working. As with the payroll factor, individuals who have traditionally been assigned to a NYS office and are now working from outside of NYS, receipts from their services will continue to be sourced to NYS unless they are assigned to an office out of NYS or establish a "bona fide" home office.

In the current environment, using the principles articulated in *Zaretsky*, it is likely that home offices established for temporary work-from-home arrangements would not be sufficient to allow for allocation of payroll and gross receipts outside of NYS. Unless businesses are able to establish more permanent and continuous offices outside of NYS, then payroll and gross receipts from services provided from temporary locations outside of NYS will likely continue to be sourced to NYS for apportionment purposes. This is because that payroll and those services will continue to be more chiefly connected to an office in NYS and not a temporary work-from-home office.

Although it may be difficult for businesses headquartered in NYS or NYC to claim home offices constitute a formal office assignment, steps may be taken to aid in establishing the continuous and permanent nature of offices outside of NYS to allow for non-NYS apportionment, in addition to the UBT recommendations above. For example, a business might:

- establish bona fide offices in locations outside of NYS where multiple partners or employees reside (such locations should be listed on company websites);
- re-assign personnel, in particular executives and senior investment professionals, to offices outside NYC, in tandem with adopting policies that implement a more permanent remote work environment;
- re-domicile funds, subsidiary investment vehicles and side-pockets outside NYS; and/or
- move investor relations and fundraising activities outside NYS.

Each of these steps can aid in taking the position that work is being performed from an office outside NYS.

In all cases, it will be important to adjust human resource documents and other internal records to reflect the establishment of new offices and/or work-from-home offices. Partners and employees should be officially assigned to their respective locations outside of NYS and be presented to clients as providing their services from those locations. Website bios, client alerts, and business cards should all be updated to include non-NYS office locations. As under the UBT, businesses should take the same or similar steps to document these new work locations; NYS will not simply take a business's word for work locations and services performed from those locations.

With respect to the property factor, in the short-term, businesses should consider maintaining any documentation related to providing computers, desks, and other equipment to allow employees to work from home. Over the long-term, the creation of new offices in locations where individual partners or investment professionals or others have relocated together with the downsizing of space in New York may meaningfully impact the property factor's NYS percentage.

C. COLLATERAL CONSIDERATIONS

When sourcing income away from NYC or NYS, it is necessary to consider where that income is being attributed and whether those other jurisdictions will subject it to tax.

Because many jurisdictions have different methods of sourcing income, it is not necessarily the result that sourcing income away from NYC and NYS, under the rules of NYC and NYS, means sourcing it to another state for tax in that state. From a remote work prospective, many of the nonresident employees and principals that are connected to NYS and NYC offices live in New Jersey and Connecticut. Under current law, the New Jersey gross income factor applies language similar to that of the PIT, which would focus more on an assigned office location than a remote work location for sourcing purposes. Accordingly, adjusting for actual place of performance under the UBT would not necessarily lead to a reallocation of income to New Jersey under its apportionment standard. Connecticut applies a market-based approach and therefore would not take remote locations into account anyway. Connecticut also has significantly lower tax rates than New York and is an attractive location for a new office. Overall, most states have a lower rate than New York, so allocating more income to another state should not represent an increased cost, even more so now that NYS increased its rates for high-income individuals and families. NYS is, in particular, imposing higher personal income tax rates than its neighbor New Jersey.

This means that adjusting UBT calculations for remote work locations presents an overall benefit that, when properly documented, is very hard for NYC to deny. PIT calculations are not so easily adjusted, but new offices that are closer to home for highly paid personnel could draw income away from NYS while also allowing for remote work flexibility.

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And for any legal questions related to this pandemic, please contact the authors of this Legal Update or Mayer Brown's COVID-19 Core Response Team at FW-SIG-COVID-19-Core-Response-Team@mayerbrown.com.

Coming Next:

Current New York Tax Considerations for Asset Managers—Part 2, Remote Work Opportunities at the Partner Level

For more information about the topics raised in this Legal Update, please contact any of the following lawyers.

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Endnotes

[1] NYC Admin. Code § 11-501(k).
[2] NYC Admin. Code § 11-501(m).
[3] NYC Admin. Code § 11-508(a).
[4] NYC Admin. Code § 11-508(c).
[5] NYC Admin. Code § 11-508(i)(1).
[6] NYC Admin. Code § 11-508(c).
[7] NYC Admin. Code § 11-508(e-3).
[8] NY Tax Law § 612(a); 20 NYCRR § 112.1.
[9] NY Tax Law § 601(e).
[10] 20 NYCRR § 132.15.
[11] 20 NYCRR § 132.15(f).
[12] 20 NYCRR § 171.6(b)(1)(ii); TSB-M12(5)I (July 5, 2012).
[13] 20 NYCRR § 132.18, *see also,* "My primary office is inside New York State, but I am telecommuting from outside of the state due to the COVID-19 pandemic. Do I owe New York taxes on the income I earn while telecommuting?" New York State Department of Taxation and Finance, Frequently Asked Questions, https://www.tax.ny.gov/pit/file/non-resident-faqs.htm#telecommuting.
[14] NYC Admin. Code § 11-508(c)(3).
[15] NYC also eliminated the alternative books and records method for sourcing gross income.
[16] NYC Admin. Code § 11-508(c).
[17] RCNY 11-65(b)(3)(i).
[18] *See In the Matter of Gerson Lehrman Group, Inc. v. N.Y.C. Tax App. Trib.*, 2021 N.Y. Slip Op. 2102 (N.Y. App. Div. 2021).
[19] *Id.*
[20] *See* TSB-A-95(11)C (July 26, 1995).
[21] *Matter of Gerson Lehrman, supra note 18.*
[22] *S&P Global Inc. f/k/a McGraw Hill Financial, Inc. v. N.Y.C. Tax App. Trib.*, 48 NYS3d 346 (N.Y. App. Div. 2017).
[23] NYC Admin. Code § 11-502(c).
[24] NY Tax Law § 601(f); 20 NYCRR § 132.15(a).
[25] NY Tax Law §§ 601(e), 612, 620(a).
[26] NY Tax Law §§ 601(e), 631(c), 632(a)(1).
[27] 20 NYCRR § 132.15.
[28] 20 NYCRR § 132.15(e).
[29] Form IT-203-A, *Business Allocation Schedule*.
[30] 20 NYCRR § 132.15(f).
[31] *Id.*
[32] New York City Finance Letter Ruling, No. 02-4792 (June 18, 2002).
[33] *Matter of Zaretsky*, FHD(363)-UBT-6/91(0-0-0) (NYC Dept. of Fin. Hearing June 28, 1991).
[34] N.Y. Tax Law § 631(b)(2).