

**New York State Department of Taxation and Finance
Office of Counsel
Advisory Opinion Unit**

TSB-A-15(5)I
Income Tax
May 29, 2015

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. 1140128A

The Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED] (“Petitioner”), a non-resident of New York State, sold stock in a New York Subchapter S corporation to the S corporation under a stock redemption plan and received an installment note as part of the stock sale. Petitioner asks whether the gain on the redemption of the stock and the interest income on the installment note payments are subject to New York State personal income tax.

We conclude that the interest paid to Petitioner pursuant to the installment note is not subject to New York State personal income tax. However, a portion of the gain on Petitioner’s stock that was included in the principal payments on the installment note would be attributable to an interest in real property in New York and would be New York source income subject to New York State personal income tax, if the conditions in Tax Law § 631(b)(1)(A)(1) are met.

Facts

Petitioner inherited stock in an S corporation operating in New York State. The S corporation, which made the New York S election, owns New York State real estate and derives 69% of its income from an active parking operation and 31% from real estate rentals. The company has been in business for over 20 years and has no plans to liquidate. In 2012, Petitioner, who has been a resident of Georgia since 1997 and has never been active in the business, sold her entire 33% interest in the S corporation back to the S Corporation pursuant to a stock redemption plan and received an installment note from the S Corporation as part of the stock sale. Petitioner asks whether the gain from the stock redemption and the interest income on installment note payments are subject to New York State personal income tax.

Analysis

Generally, a nonresident of New York is subject to New York State personal income tax on his or her New York source income that enters into his or her federal adjusted gross income (FAGI). *See* Tax Law § 631(a). New York source income is defined as the sum of income, gain, loss, and deduction derived from or connected with New York sources. *See* Tax Law §

631(b)(1). Those tax items include items attributable to the ownership of any interest in real property located in this state. *See* Tax Law § 631(b)(1)(A). The term “real property located in this state” includes an interest in an S corporation that owns real property in New York, if the real property in New York has a fair market value that equals or exceeds 50% of the value of all the assets of the entity on the date of the sale that were owned for a least two years before the date of the sale of the S Corporation’s stock. *See* Tax Law § 631(b)(1)(A)(1). Thus, if the valuation conditions in § 631(b)(1)(A)(1) are met, a portion of the gain on the redemption of Petitioners’ stock in the S corporation, reflected in the principal payments of the installment note, would be New York source income and subject New York State personal income tax. The portion of the gain that constitutes New York source income would be determined by multiplying the amount of the gain by a fraction, the numerator of which is the fair market value of the New York real property on the date of the sale or exchange and the denominator of which is the fair market value of all of the entity’s assets (owned for at least two years) on the date of the sale or exchange. To the extent that this gain is paid to the taxpayer under an installment payment agreement, a portion of each installment payment would be New York source income.

Items of income, gain, loss, and deduction attributable to intangible personal property, including interest and gain from the disposition of intangible personal property, shall constitute income derived from New York sources only to the extent that such income is from property employed in a business, trade, profession, or occupation carried on in New York. *See* Tax Law § 631(b)(2). Generally, where a nonresident individual sells real or tangible personal property located in New York State and, as a result of such sale, receives as payment intangible personal property, *e.g.*, a note, that generates interest income, such interest income is not attributable to the sale of the property but is attributable to nontaxable intangible personal property. *See* 20 NYCRR § 132.5(b).

In *Matter of Epstein v. State Tax Commission*, 89 A.D.2d 256 (1982), the taxpayers, who were nonresidents of New York during the taxable years in question, sold an apartment building located in New York and took back a purchase-money mortgage for the unpaid balance of the purchase price. The note provided for interest at the rate of 6% per annum with quarterly payments of principal and interest. The Appellate Division concluded that the income-producing personal property was the mortgage note, *i.e.*, intangible personal property, and not the real estate apartment building, and thus the interest income was not taxable. However, with regard to the amount of principal payments included on the mortgage installments, the amounts that represented gains on the sale of the stock were reported correctly as nonresident New York State personal income. *See also, Delmhurst v. State Tax Commission*, 92 A.D.2d 981(1983); *Katz v. State Tax Commission*, 110 A.D.2d 1029 (1985).

Thus, we conclude that the interest on the installment note that Petitioner receives in exchange for the stock is not income attributable to property employed in a business, trade, profession, or occupation carried on in New York and as such is not subject to New York State personal income tax. However, a portion of the gain on Petitioner’s stock that is included in the principal payments on the installment note is attributable to an interest in real property in New

York and would be New York source income subject to New York State personal income tax, if the valuation conditions in Tax Law § 631(b)(1)(A)(1) are met.

DATED: May 29, 2015

/S/

DEBORAH R. LIEBMAN
Deputy Counsel

NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion. The information provided in this document does not cover every situation and is not intended to replace the law or change its meaning.