

State and Local Tax ADVISORY

August 28, 2012

Significant Development in New York: New York Supreme Court Strikes Down MTA Payroll Tax

In a recent decision, the New York Supreme Court held that the Metropolitan Commuter Transportation Mobility Tax (“MTA payroll tax”) was passed unconstitutionally and thus is invalid.¹ This decision potentially impacts all companies with operations in the New York City area and its development should be closely monitored. The MTA payroll tax was passed by the New York legislature in May 2009 to address a projected \$1.8 billion gap in the MTA’s annual budget.² The MTA payroll tax is a graduated tax ranging from .11 percent - .34 percent and is imposed on employers operating within the Metropolitan Commuter Transportation District, which includes all of New York City and seven surrounding counties,³ and having payroll expenses exceeding \$312,500 during the calendar quarter. The tax is computed by multiplying the employer’s payroll expense by the applicable rate.

In *Mangano, et al. v. Silver, et al.*, several of the local governments within the District filed suit, challenging the validity of the tax by asserting, *inter alia*, that its passage violated Article IX of the New York State Constitution (the “Home Rule provision”), which provides that a special law relating to the property, affairs or government of any local government may not be enacted without a vote of two-thirds of the total membership of the legislative body of the counties affected by the law.⁴

After determining that the law is a “special law” in that “payroll tax applies to counties, but not all counties in the state,” the court agreed with the local governments in finding that its passage violated the Home Rule provision, because no home rule message was provided by the affected localities.

The court also noted that although the Home Rule provision may be avoided where the passage of a law serves a “substantial state concern,” the MTA payroll tax did not bear a reasonable relationship to a substantial state concern because it is not imposed state-wide—it only taxes employers located within the district. The court concluded that “it is hard to see how the residents in Buffalo or other upstate areas would” be affected by a decrease in the capability of the MTA and that if there was substantial state concern, then the legislature could have presumably taxed every county within the

¹ *Mangano, et al. v. Silver, et al.*, Index No. 144440/10 (N.Y. Sup. Ct. Aug. 22, 2012).

² Codified at N.Y. Tax Law § 801(a).

³ Affected counties include Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk and Westchester.

⁴ N.Y. Const., art. IX, § 2(b)(2).

state. Therefore, the court concluded that the budgetary crisis of the MTA is not a matter of substantial state concern and the exception to the Home Rule provision did not apply.

Implications of the Decision

Though the Mangano Court held the MTA payroll tax unconstitutional, the MTA has indicated that it intends to appeal the decision, stating that four prior challenges to the constitutionality of the law making the same argument have been dismissed.⁵ The MTA has indicated that the state will continue to collect the tax pending appeal and the New York State Department of Taxation and Finance has issued informal guidance stating that taxpayers should continue to pay the tax and file returns.⁶ Any appeal may focus on whether a disruption to the MTA and its operations would amount to a substantial state concern, which would allow it to bypass the rule requiring a home rule message.

These open issues surrounding the efficacy of this opinion should be considered by companies in deciding whether to file refund claims for open periods, including whether to file a protective refund claim, as well as in determining whether to pay the MTA payroll tax going forward.

Please contact any one of our New York-based state and local tax attorneys, or any other member of our State and Local Tax Group, to discuss this decision and its application to your business.

⁵ Joan Gralla, *New York's MTA Payroll Tax Unconstitutional*: Judge, Reuters, <http://www.reuters.com/article/2012/08/23/us-usa-newyork-mta-tax-idUSBRE87M03820120823> (Aug. 22, 2012).

⁶ <http://www.tax.ny.gov/bus/mctmt/default.htm> (last accessed Aug. 27, 2012).

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