

Income/Franchise:

New York City: Commission Payments to Federal “DISC” Held as Nondeductible for UBT Purposes

TAT(E)17-21(UB), N.Y.C. Tax App. Trib. (1/26/23). In a ruling involving a limited liability partnership (LLP) that made payments in the form of commissions to a federally-recognized domestic international sales corporation (DISC) with no employees and whose shareholders were all partners in the LLP, the New York City Tax Appeals Tribunal (Tribunal) affirmed that based on the provided facts, the payments were made to the LLP’s partners for their services and thus were nondeductible for New York City (City) Unincorporated Business Tax (UBT) purposes pursuant to City law that bars deductions for amounts paid or incurred to a proprietor or partner for services or the use of capital. The Tribunal explained that the “Third-Party Payment Rule” in the UBT regulations applied to the commissions paid to the DISC in this case. Specifically, the LLP paid the commissions to DISC for the benefit of the partners; the LLP received a tax deduction for the payment, and the partners received their share of the commissions from the DISC at a reduced tax rate (*i.e.*, as distribution treated as a dividend for federal tax purposes); and the commissions compensated the partners for their services to the LLP in connection with services performed. All the requirements of UBT Rule 28-6(d)(1)(i)(B), therefore, were satisfied, and the third-party commission payments were not deductible. Referencing the administrative law judge’s earlier ruling in this case, the Tribunal agreed that the payment for a portion of the partners’ compensation into a DISC to secure a tax benefit is “no different than the deductions we have previously denied for contributions made on behalf of partners or sole proprietors to defined benefit retirement plans and health plans.” Please contact us with any questions.

URL: <https://www.nyc.gov/assets/taxappeals/downloads/pdf/1721DEC0123.pdf>

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