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NEW YORK CITY DEPARTMENT OF FINANCE

UPDATE ON AUDIT ISSUES

UBT

Unincorporated Business Tax
Payments to Partner/Proprietor

June 2006

I. ISSUE

Whether payments made to a partner or proprietor for services or for the use of capital are deductible for Unincorporated Business Tax (UBT) purposes.

NYC allows an Unincorporated business entity (partnership, LLC or individual) a standard exemption and an allowance for services in computing its taxable income. No other amounts paid to a partner or proprietor for services or the use of capital are deductible.

I. CITE AND EXPLANATION

NYC Administrative Code Sec. 11-507 (3) and Rule Section 28-06 states that "No deduction shall be allowed...for amounts paid or incurred to a proprietor or partner for services or for use of capital."

Examples:

- a. A sole proprietor who does his own bookkeeping, billing, and other administrative services may not deduct the cost of his time and skill in providing such services.
- b. Salaries, commissions, consultant fees, or professional fees paid to a general or limited partner for personal services rendered by the partner, either as an employee or as an independent contractor of the unincorporated business, may not be deducted by the partnership.
- c. Fixed annual payments made to retired partners under the terms of the partnership agreement, although deductible as "guaranteed payments" for federal income tax purposes, may not be deducted.
- d. Interest paid to a general or limited partner for monies contributed or loaned to the partnership may not be deducted by the partnership.
- e. A sole proprietor may not claim a rental expense for the use of real property he/she owns.

Rule Section 28-06 further provides and summarizes that:

- a. Amounts paid to or incurred by a corporate partner for services provided to the unincorporated business by the partner's officers shall not be allowed as a deduction. Corporate officers include the chairman, president, vice-president, secretary, asst. secretary, treasurer, asst. treasurer, comptroller or any other individuals charged with performing executive duties of the corporation. Payments made or incurred for services performed by an individual who is both an officer and an employee are also not deductible.
- b. Amounts paid to or incurred by a partnership which is a member partner in an unincorporated business for services provided by a partner of the member partnership are not deductible.

I. RECOMMENDATION

Even though payments to partners are deductible for federal tax purposes, they are not deductible for Unincorporated Business Tax purposes and should added back when preparing the return.