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Diana Beinart
General Counsel/Deputy Commissioner

July 10, 2020

XXXXXX
XXXXXX

RE: Request for Letter Ruling
Unincorporated Business Tax
FLR 20-5002

Dear Taxpayer:

This is in response to your request dated November 21, 2019 for a ruling regarding the applicability of the New York City Unincorporated Business Tax (“UBT”) to two entities, XXXXXX (“Management”) and XXXXXX (“Investments”), upon the sale of all membership interests in Investments, in the transaction described below.

You have submitted the following documents with your request (1) Operating Agreement of Management; (2) Limited Liability Company Agreement of Investments; (3) all federal, state and local tax returns filed on behalf of Management for tax years 2016-2018; and (4) all federal, state and local tax returns filed on behalf of Investments for tax years 2016-2018. The Development Agreement between Investments and XXXXXX was submitted on May 3, 2020.

FACTS

The pertinent facts presented by the Taxpayer are as follows:

In 2015, XXXXXX (“Developer”) entered into negotiations with XXXXXX (“Tenant”) for the construction and subsequent leasing by Tenant of a commercial facility on property located in Queens, NY. Developer formed Investments in May of 2016 and Investments purchased the land on which the facility was to be constructed. Investments entered into a contract with Developer providing that Developer would, in consultation with Investments, initiate, coordinate and administer all planning, design and construction activities for all improvements related to the completion of the commercial facility. Construction was completed in 2017 and the lease agreement between Tenant and Investments commenced. Since the completion of the project and commencement of the lease,

Investments has not engaged in any activity except collecting rent amounts under the lease agreement with Tenant.

Management, along with two other LLCs (XXXX and XXXX) collectively own Investments. Management is owned by two individuals and an LLC, which is a disregarded entity of an individual. Management was a vehicle through which the upper level management of Developer would participate in the equity of the construction and leasing of the commercial building owned by Investments. It did not derive any fees or perform any services.

In 2019, all of the members of Investments exercised an option to sell their interest in Investments to XXXXXX (“Acquisitions”), a company owned by XXXXX. Under federal tax law Investments became a disregarded entity for federal income tax purposes and the sellers were considered to have sold their member interests, but Acquisitions was deemed to have purchased Investments’ assets.

ISSUES

1. Whether Investments will recognize gain on the sale of the membership interests by its members?
2. Whether Management will be subject to the UBT on the gain realized from the sale of their membership interest in Investments?

CONCLUSIONS

1. Investments will not recognize gain on the sale of its members’ ownership interests.
2. Management is not subject to the UBT.

DISCUSSION

1. No gain recognized by Investments on the sale of membership interests by its members.

Section 11-503(a) of the Administrative Code of New York City (“the Code”) imposes the UBT on the unincorporated business taxable income (“UBI”) of every unincorporated business carried on within New York City. A taxpayer’s UBI is computed by reducing its unincorporated business gross income (determined under Code section 11-506) by its allowable unincorporated business deductions (determined under Code section 11-507). The unincorporated gross income of an unincorporated business, is defined in pertinent part as

“...[T]he sum of the items of income and gain of the business, of whatever kind and in whatever form paid, includible in gross income for the taxable year for federal purposes, including income and gain from any property employed in the business, or from the liquidation of the business.”¹

For federal purposes, under Internal Revenue Code (“IRC”) section 741, the gain or loss from the sale or exchange of an interest in a partnership is recognized by the transferor partner. Therefore,

¹ Ad. Code Section 11-506(a).

any gain or loss on the sale or transfer of a partnership interest in Investments would not be attributable to the LLC itself and would not be includable in their UBI per the definition of unincorporated gross income under the Code.

2. Management is not subject to the UBT.

As noted above, under IRC section 741 the gain or loss from the sale or exchange of an interest in a partnership is recognized by the transferor partner. Therefore, Management as the transferor partner would recognize the gain or loss from the sale of their partnership interest in Investments. Whether such gain will be subject to taxation under the UBT depends on whether Management is considered to be carrying on a taxable unincorporated trade or business within the City under the UBT Code provisions and the applicable rules.

“In general the trades, businesses, professions or occupations which constitute an unincorporated business when conducted, engaged in or being liquidated by an individual or an unincorporated entity include, without limitation,...any other activity which involves the leasing of or trading or dealing in real or personal property...”² However, an individual or other unincorporated entity (except a dealer) will not be deemed engaged in an unincorporated business solely by reason of the acquisition, holding or disposition, other than in the ordinary course of business of an interest in unincorporated entities engaged solely in the purchase, holding and sale of property for their own accounts and any other activity not otherwise constituting the conduct of an unincorporated business subject to the tax, otherwise referred to as the full self trading exemption.³ Investments was solely engaged in activity not constituting an unincorporated business subject to the tax. Therefore, under Code 11-502(c)(2)(B) Management would not be deemed to be engaged in an unincorporated business solely by the holding and disposition of an interest in Investments.

This letter ruling makes no determination as to any potential UBT consequences to either the other owners of Investments, the owners of Management or Developer. DOF reserves the right to verify the information submitted. Please advise DOF of any material change in the facts presented.

Sincerely,

Diana Beinart
General Counsel

CCS:ccs

² RCNY 28-02(a)(5).

³ Ad. Code 11-502(c)(2).