

This Week in State Tax (TWIST)

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New York: Tribunal Reverses ALJ on Distortion, but Affirms on Sourcing Investment-Related Receipts

The New York Tax Appeals Tribunal (Tribunal) reversed the portion of a taxpayer's recent victory that related to look-through sourcing of broker-dealer income. The taxpayer, an investment bank, was parent of a combined group that included multiple registered broker-dealers. The taxpayer initially filed its New York combined returns for the relevant years by sourcing receipts of these subsidiaries based on the location of their direct contractual counterparts—the financial intermediaries such as pensions and mutual funds (the funds") to which the broker-dealers provided investment services. It later amended the returns to source the receipts using U.S. census data as an approximation of the locations of the funds' underlying investors (who, the taxpayer argued, ultimately bore the economic burden of the transactions).

For the years at issue, New York law generally required broker-dealer receipts to be sourced to the location of the customer to whom the broker-dealers services were provided. The Division of Taxation (Division) rejected the resulting refund, and the taxpayer appealed. On review, an Administrative Law Judge (ALJ) agreed with the taxpayer that underlying investors of the institutional intermediaries were the ultimate payers for the services, but further found that state law did not provide for look-through sourcing to the underlying investor. The ALJ went on to hold, however, it was unreasonable of the Division to refuse to exercise its discretionary authority given the level of distortion caused by the statutory sourcing method.

On appeal by the Division, the Tribunal reversed the ALJ's determination and found that the institutional investors were the customers of the broker-dealers, and the statute accordingly required sourcing of the receipts using the mailing addresses of the institutional intermediaries. The Tribunal determined that, under the sourcing rules for the years at issue, looking through the institutional intermediaries to underlying investors was not a permitted sourcing method. The Tribunal disagreed with the ALJ's conclusion that sourcing based on the intermediaries would be impermissibly distortive, holding that there is no constitutional violation when the receipts are applied per the statute in the case of this taxpayer. The Tribunal did affirm certain aspects of the ALJ decision concerning matters other than sourcing. Please contact [Russell Levitt](#) or [Aaron Balken](#) with questions on [Matter of Jefferies Group LLC & Subsidiaries and its continuing relevance to current New York law](#).

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