

# SCOTUS Rejects New York Royalty Exclusion Challenge by Disney, IBM

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By Andrea Muse

The U.S. Supreme Court will not take up the constitutional challenge to New York's foreign royalty addback provision brought by Walt Disney Co. and IBM Corp.

In a [January 21 order](#), the Court denied the companies' certiorari petitions in *The Walt Disney Co. v. New York Tax Appeals Tribunal* and *International Business Machines Corp. v. New York Tax Appeals Tribunal*, which argued that the denial of deductions for royalty payments received from foreign affiliates violates the internal consistency test and discriminates against interstate and foreign commerce.

"The petitions for cert. were powerful and made out a compelling case," University of Connecticut law professor Richard Pomp told *Tax Notes*. But he said that the issue in New York had no ongoing significance because the law had been changed.

However, Pomp said that "the underlying issue will rear its head elsewhere and the Court will confront it again."

## Arguments to the Court

The New York Court of Appeals [held in April 2024](#) that a related member must be subject to the state's addback requirement for royalty income received by a taxpayer to be excluded from the taxpayer's entire net income. Because Disney's and IBM's foreign affiliates are non-New York filers, the court concluded that the affiliates were not required to add back the royalty payments and the companies' exclusions were properly disallowed.

New York [urged the Supreme Court](#) to deny review in the cases in December 16, 2024, briefs, noting that the challenged statute was repealed over a decade ago.

But IBM argued in a December 30, 2024, [reply brief](#) that the repeal [did not diminish](#) the importance of the legal principles at play in these cases, and Disney contended in its [December 31 reply brief](#) that hundreds of millions of dollars in tax revenue remain in dispute. The disallowance of the deductions resulted in the denial of refund claims and notices of deficiency of roughly \$4 million to Disney and \$65 million to IBM.

Under former New York Tax Law section 208(9)(o)(3), which was eliminated for tax years beginning on or after January 1, 2013, a taxpayer could exclude royalty income received from a related member from its entire net income unless the royalty payments were not required to be added back.

## *Zilka*

The companies had asked the Court to grant their cert. petitions or, alternatively, to hold their petitions pending the outcome in *Zilka v. Tax Review Board of Philadelphia* after the Court asked for the views of the U.S. solicitor general in the case, asserting that *Zilka* also involved dormant commerce clause issues.

In *Zilka*, a Philadelphia resident working in Wilmington, Delaware, challenged Philadelphia's denial of a city wage tax credit for out-of-state income taxes paid to Delaware, contending that the city was unconstitutionally discriminating against interstate commerce.

But the solicitor general argued in a [December 2024 brief](#) that the Court should not take up *Zilka*. The Supreme Court [declined to review](#) the Pennsylvania Supreme Court decision on January 13.

Timothy Noonan of Hodgson Russ LLP told *Tax Notes* in a January 21 email that he had believed it would only be a matter of time before the Court again picked up a dormant commerce clause case, as a lot more of these constitutional challenges are being seen in the state tax world.

"But as we saw a week or so ago, the Court declined to take the *Zilka* case, which probably was an even more important and more talked about case than *Disney* and *IBM*," Noonan said.

"It's not that surprising that the Court declined cert. in these cases," considering that development, Noonan said. "It may simply be less interested in commerce clause cases" regarding state and local tax than practitioners, he said.

Lawyers for IBM declined to comment. The companies, the lawyers for Disney, and the New York attorney general's office did not respond to requests for comment by press time.

In *The Walt Disney Co. v. New York Tax Appeals Tribunal* (Case No. 24-333), Disney was represented by Marc A. Simonetti and Rick Capossela of State Tax Law LLC; and Paul Clement, Matthew D. Rowen, and Nicholas M. Gallagher of Clement & Murphy PLLC.

In *International Business Machines Corp. v. New York Tax Appeals Tribunal* (Case No. 24-332), IBM was represented by Jeffrey A. Friedman, Ted W. Friedman, and Jeremy P. Gove of Eversheds Sutherland (US) LLP; and Yaakov M. Roth, Brendan D. Duffy, and Traci L. Lovitt of Jones Day.