

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
JANE A. MALLINCKRODT	:	DECISION
for Redetermination of a Deficiency or for	:	DTA No. 807553
Refund of Personal Income Tax under Article 22	:	
of the Tax Law and Chapter 46, Title T, of the	:	
Administrative Code of the City of New York for	:	
the Years 1983 and 1984.	:	

Petitioner Jane A. Mallinckrodt, c/o Anderson Trading, Inc., 900 Third Avenue, 12th Floor, New York, New York 10022 filed an exception to the determination of the Administrative Law Judge issued on February 27, 1992 with respect to her petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law and Chapter 46, Title T, of the Administrative Code of the City of New York for the years 1983 and 1984. Petitioner appeared by the Law Offices of Bryan Cave (Juan D. Keller, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Andrew J. Zalewski, Esq., of counsel).

Petitioner filed a brief on exception. The Division of Taxation filed a letter in lieu of a brief in opposition to petitioner's exception. Petitioner filed a letter in response to the Division of Taxation's letter.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUES

I. Whether it was an error for the Administrative Law Judge, acting on her own initiative, to disregard the stipulation of the parties that trust income received by petitioner was taxed by the State of Missouri.

II. Whether income received by petitioner from trusts created in Missouri and administered in Missouri by a Missouri trustee was "derived" from Missouri within the meaning of Tax Law § 620.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Petitioner, Jane A. Mallinckrodt, timely filed New York State and City resident income tax returns for 1983 and 1984. On each return, she claimed a resident tax credit for income taxes paid by her to the State of Missouri.

On May 5, 1986, the Division of Taxation ("Division") issued to petitioner a Statement of Audit Changes for the years 1983 and 1984, making several adjustments to petitioner's calculation of income tax for those years. The only adjustment relevant to this determination is the Division's disallowance of the resident tax credits. The Division provided the following explanation for the disallowance: "A resident credit cannot be allowed for taxes paid to another state on income from intangible personal property including dividends, interest, and gains from the disposition of intangible personal property." The statement shows a total amount due for 1983 and 1984 of \$62,798.00, consisting of a tax deficiency of \$19,487.00 and a penalty under Tax Law § 685(c) of \$1,593.00 for 1983 and a tax deficiency of \$41,418.00 for 1984. The \$300.00 balance represents an addition error.

On August 11, 1987, the Division issued to petitioner a Notice of Deficiency for the years 1983 and 1984, asserting a combined New York State and New York City tax deficiency of \$62,798.00 plus interest.¹

¹The Statement of Audit Changes shows the imposition of a penalty of \$1,593.00 under section 685(c) of the Tax Law for the year 1983. This amount was included in the Division's calculation of the tax deficiency of \$62,798.00 and was not separately stated as a penalty. Petitioner has requested cancellation of all tax, penalty and interest asserted by the notice of deficiency. Attached to petitioner's 1983 New York State income tax return is a letter from Burke & Burke on behalf of petitioner, enclosing a check in the amount of \$39,582.00 representing tax, interest on late payment and penalty for underpayment of estimated tax in the amount of \$1,593.00

The Division and petitioner executed a Stipulation of Facts which is adopted here above, except that references to exhibits, have been omitted.

Jane A. Mallinckrodt (hereinafter "Petitioner") was an income beneficiary during the Petitioner's taxable years of 1983 and 1984 of trusts (hereinafter collectively referred to as the "Trusts") established under will or pursuant to intervivos conveyance.

The Trusts are either intervivos trusts created by Missouri residents or testamentary trusts probated in the State of Missouri.

The Trusts are Missouri resident trusts properly administered and taxed pursuant to Missouri State law.

The Trusts (except the Arcadian Trust; Trust No. 55607-00-6) filed U.S. Fiduciary Income Tax Returns and Missouri Fiduciary Income Tax Returns for the Trusts' taxable years ending in 1983 and 1984.

Centerre Trust Company ("Centerre") was trustee or custodian of the Trusts during calendar years 1983 and 1984.

Centerre, a Missouri banking corporation, was not authorized to administer trusts in the State of New York during 1983 and 1984.

For the Trusts' taxable years ending in 1983 and 1984, the Trusts received dividend and interest income on stock, bonds and other evidence of indebtedness held by the Trusts.

The Petitioner reported her distributive share of dividend and interest income earned by the Trusts and taxable by the State of Missouri on her Missouri State Individual Income Tax Returns for the 1983 and 1984 taxable years in the amount of \$829,075 and \$923,373 respectively.

The Petitioner paid income tax to the State of Missouri on her distributive share of the dividend and interest income earned by the Trusts and taxable by the State of Missouri equal to \$38,078 for the Petitioner's 1983 taxable year and \$41,718 for the Petitioner's 1984 taxable year.

The Petitioner was a resident of the State of New York during calendar years 1983 and 1984.

The Petitioner reported her distributive share of dividend and interest income earned by the Trusts and taxable by the State of New York on her New York State income tax returns for her 1983 and 1984 taxable years in the amount of \$775,126 and \$818,825, respectively.

The facts contained in the Affidavit of Charles H. Wyers are a true account of the expected testimony of Charles H. Wyers if he would be called as a witness in the current proceeding.

Mr. Wyers was employed by Centerre as an administrator of the Trusts in 1983 and 1984. By his affidavit, Mr. Wyers states, inter alia: "The statements attached to the 1983 and 1984 U.S. Fiduciary Income Tax Returns for each Trust evidences the correct reporting of Jane Anderson Mallinckrodt's distributive share of income earned by the Trusts and taxable by the State of Missouri on her Missouri State Individual Income Tax Returns for her 1983 and 1984 taxable years in the amount of \$829,075 and \$923,373 respectively."

The Missouri individual income tax returns filed by petitioner do not clearly indicate whether petitioner filed as a resident or nonresident of Missouri in 1983 and 1984.

OPINION

In the determination below, the Administrative Law Judge held that petitioner was not entitled to the resident tax credit contained in Tax Law § 620 for taxes paid to the State of Missouri in 1983 and 1984 on two grounds. First, the Administrative Law Judge held that petitioner had failed to prove that the State of Missouri imposed a tax on the subject income for the years at issue. In addition, the Administrative Law Judge held that the income from trusts, upon which the tax was paid, was not "derived" from Missouri as required in Tax Law § 620(a).

In her exception, petitioner makes the following arguments: 1) that the nexus between the State of Missouri and the income earned by the trusts satisfy the requirement of the section 620 credit that the trust income be derived from the state to which tax on that income is paid; 2) that allowance of the tax credit under section 620(a) for the taxes paid to the State of Missouri is consistent with the legislative intent to preclude double taxation of the same income; 3) that the parties' stipulation that the trust income was taxable in Missouri precluded the Administrative Law Judge from resurrecting this issue on her own initiative; and 4) that denial of the tax credit

would violate the Commerce Clause of the United States Constitution, as it would unfairly disadvantage trust administrators outside New York State.

In response, the Division states that the New York source rules contained in its regulations, which explicitly govern the facts of this case, deny the credit. The Division contends that petitioner proposes an expansive interpretation of section 620(a) that is not permitted by the applicable regulation.

We affirm the determination of the Administrative Law Judge.

Tax Law § 620(a) provides, in pertinent part, that:

"[a] resident shall be allowed a credit against the tax otherwise due under this article for any income tax imposed for the taxable year by another state of the United States . . . upon income both derived therefrom and subject to tax under this article."

Therefore, petitioner must prove three elements in order to receive a credit for tax paid to Missouri: 1) that Missouri imposed a tax on the subject income; 2) that the income was derived from Missouri; and 3) that the income was subject to tax under Article 22 of the New York Tax Law. It is not disputed that the third requirement is met, as the trust income was taxable by New York under Tax Law § 612(a) by virtue of petitioner's New York resident status during the years in issue.²

As to the first requirement that Missouri imposed a tax on the subject income, the parties stipulated to the following:

"[t]he Petitioner paid income tax to the State of Missouri on her distributive share of the dividend and interest income earned by the trusts and taxable by the state of Missouri equal to \$38,078 for the Petitioner's 1983 taxable year and \$41,718 for the Petitioner's 1984 taxable year" (see, Exhibit "H," emphasis added).

Despite this stipulated fact, the Administrative Law Judge sustained the denial of the credit on the ground that petitioner had failed to prove that the trust income was taxable by Missouri. Specifically, she held that this stipulated fact does not establish on what basis petitioner was required to file and pay Missouri income tax on her share of the income from the trusts. On

²Tax Law § 612(a) states that "[t]he New York adjusted gross income of a resident individual means his federal adjusted gross income as defined in the laws of the United States for the taxable year [with modifications not relevant here]."

exception, petitioner argues both that the stipulation between the Division and petitioner clearly provides that the income earned by the trusts was taxable by the State of Missouri, and that it was an error for the Administrative Law Judge to raise this issue on her own initiative. We agree with petitioner on this issue.

The Tribunal's Rules of Practice and Procedure provide guidance in examining the propriety of the Administrative Law Judge's ruling. Regulation 20 NYCRR 3000.7(a)(1)(i) states that:

"[w]ith the exception of those instances where the petitioner does not desire to stipulate any facts, the parties are required to stipulate, to the fullest extent to which complete or qualified agreement can or fairly should be reached, all facts not privileged which are relevant to the pending controversy."

Regulation 20 NYCRR 3000.7(e) states, in part, that:

"[t]he tribunal, administrative law judge or presiding officer will not permit a party to a stipulation to qualify, change or contradict a stipulation in whole or in part, except where justice requires."

We find these rules, which aid in narrowing the scope of litigation to only those disputed issues, to apply with equal force to issues raised by the Administrative Law Judge. Because the terms of a stipulation may not be later rejected by a party except in a rare case, we hold it to be axiomatic that the Administrative Law Judge may not strike a stipulation sua sponte where she would possess no discretion to take such action at the behest of a party.

This holding is consistent with the position recently taken by the United States Court of Appeals for the Sixth Circuit. In Matter of Quirk v. Commissioner (928 F2d 751, 91-1 USTC ¶ 50,148), the taxpayer, a retired partner, stipulated before the Tax Court that the discharge of his share of partnership indebtedness by the partnership resulted in a "distribution" to him. Upon the Tax Court's denial of his petition, he brought an appeal under a new theory in which he claimed that the discharge of his indebtedness did not result in a "distribution." The taxpayer argued that he should not be bound by his stipulation on this issue because the amount he received as a

distribution for tax purposes was a question of law as well as of fact.³ The Court rejected the taxpayer's argument. Interpreting Tax Court Rule 91(e), the language of which is identical to that contained in Tribunal rule 3000.7(e),⁴ the Court stated:

"the Tax Court Rules of Practice and Procedure admonish litigants in that court that their stipulations generally will be treated as binding and conclusive (citing Rule 91[e]). Normally when a party wants to waive an argument or issue that might otherwise be litigated, the waiver can be accomplished by a stipulation which narrows the dispute. In fact, narrowing disputes to the essential disputed issues is the primary function of stipulations. It would seem that if parties could challenge their prior stipulations at will, stipulations would lose much of their purpose" (Matter of Quirk v. Commissioner, *supra*, 91-1 USTC ¶ 50,148 at 87,908).

In light of our reading of the above regulations, as well as our concurrence with the reasoning enunciated by the Sixth Circuit in Matter of Quirk, we hold that the Administrative Law Judge erred in disregarding the stipulated fact that petitioner's trust income was taxable in Missouri. On the basis of this stipulated fact, we conclude that the first element of the credit is satisfied, i.e., that Missouri imposed an income tax on the income in issue.

We will now address the issue of whether the trust income received by petitioner was "derived" from Missouri within the meaning of Tax Law § 620(a). Where a statute authorizes an exemption from taxation on income which is otherwise subject to tax, it will be construed against the taxpayer, although the interpretation should not be so narrow and literal as to defeat its settled purpose (Matter of Grace v. New York State Tax Commn., 37 NY2d 193, 371 NYS2d 715, lv denied 37 NY2d 708, 375 NYS2d 1027). Because a credit, like a deduction, is a particularized

³The taxpayer cited Swift & Co. v. Hocking Valley Ry. Co. (243 US 281 [1917]) for the proposition that a court cannot be controlled by agreement of counsel as to a subsidiary question of law.

⁴Rule 91(e) of the Tax Court provides:

"(e) Binding effect. A stipulation shall be treated, to the extent of its terms, as a conclusive admission by the parties to the stipulation, unless otherwise permitted by the court or agreed upon by the parties. The Court will not permit a party to a stipulation to qualify, change or contradict a stipulation in whole or in part, except that it may do so where justice requires."

species of exemption from taxation, the same rule applies to credits (see, Matter of Grace v. New York State Tax Commn., supra, 371 NYS2d 715, 719).

Petitioner contends that the requirement that the tax paid to another state be "derived therefrom" is satisfied in this case because a nexus exists between petitioner (vis-a-vis the trust property) and Missouri, which is a constitutional requirement for a state to tax. Specifically, petitioner contends that where an income-producing activity is availed the opportunities, protections, and benefits of the laws of a state, the state may constitutionally tax the income (citing Wisconsin v. J.C. Penney Co., 311 US 435, reh denied 312 US 712). Accordingly, she argues that because the trusts generating the income were administered in Missouri and, thus, were availed the opportunities, protections, and benefits of the laws of Missouri, the income was "derived" from Missouri within the meaning of section 620(a).⁵

Petitioner, in applying a constitutional nexus standard to a taxpayer vis-a-vis income received, appears to assert that the Legislature intended the credit to apply against tax imposed by a state on any income which could be constitutionally taxed. In support of her position, petitioner cites the legislative history of section 620(a), which simply states that the statute was designed to protect New York residents from being subjected to double taxation (Memoranda of State Dept. of Taxation & Fin., NY Legis Ann 1962, at 233).

In response, the Division asserts that regulation former 20 NYCRR 121(1)(d),⁶ which served as the basis for the Administrative Law Judge's decision, is a valid interpretation of section 620(a) and should govern. This regulation states:

⁵Petitioner has not explained why her argument is not equally applicable to a taxpayer who is a resident of New York as well as another state and who has paid taxes to the other state. A state's right to tax a resident's entire income is founded upon the rights and privileges received by the resident from the state (People ex rel Cohn v. Graves, 300 US 308). Thus, under petitioner's argument, a resident of New York and another state could claim that all of his income was derived from the other state because the individual benefited from the rights and privileges of being a resident of the other state. Although this specific argument was not addressed, the application of the credit in such a situation has been rejected (see, Matter of Leach v. Chu, 150 AD2d 842, 540 NYS2d 596, appeal dismissed in part, denied in part 74 NY2d 839, 546 NYS2d 344 [Connecticut domiciliary denied credit under section 620(a) on Connecticut taxes paid, for failure to establish that subject income was "derived" from Connecticut]).

⁶This was changed to 20 NYCRR 120.4(d) effective February 29, 1992.

"the resident credit against ordinary tax is allowable for income tax imposed by another jurisdiction upon compensation for personal services performed in the other jurisdiction, income from a business, trade or profession carried on in the other jurisdiction, and income from real or tangible property situated in the other jurisdiction. On the other hand, the resident credit is not allowed for tax imposed by another jurisdiction upon income from intangibles, except where such income is from property employed in a business, trade or profession carried on in the other jurisdiction. Thus, for example, no resident credit is allowable for an income tax of another jurisdiction on dividend income not derived from property employed in a business, trade or profession carried on in such jurisdiction" (emphasis added).

At the outset, we note that our decision is not governed by constitutional principles, but, rather, by statutory interpretation. The Due Process Clause does not prohibit the double taxation that can arise from the concurrent power possessed by the state of the taxpayer's residence and another state with which the taxpayer or his property has contact to tax the income of the taxpayer or his property (see, Curry v. McCannless, 307 US 357; see also, State Tax Commn. of Utah v. Aldrich, 316 US 174). Thus, the granting of a credit in this instance is not constitutionally required, but simply a matter of legislative grace (see, Matter of Grace v. New York State Tax Commn., *supra*). An administrative agency's role in drafting regulations is to explain and clarify legislation in accordance with the intention of the Legislature which enacted it. Therefore, when determining the validity of 20 NYCRR 121(1)(d), a critical question is whether it comports with the legislative intent of section 620.

Petitioner argues that there is no basis for treating income from a trust differently from income from a business, trade or profession conducting its activities in Missouri. She argues that the trusts, like a business, trade, or profession, received the benefits, privileges, and protections of the State of Missouri in conducting their administrative and income-producing activities in Missouri -- thereby establishing a taxing nexus between the State of Missouri and the income generated by the trusts.

Under former 20 NYCRR 121.4(d), the income qualifying for the credit is as follows: 1) income derived from a business, trade or profession carried on in the taxing state; 2) income from real or tangible personal property situated in the taxing state; and 3) income from

intangibles where such income is from property employed in a business, trade or profession. The Division, in drafting this regulation, interpreted the word "derived" in section 620(a) to require a more substantial degree of contact with the taxing state than might be sufficient to grant that state the ability to constitutionally tax the income. Under the regulation, the contact is sufficient only where the income arises from either the taxpayer's commercial activities within the state or from real or tangible property situated therein.

By contrast, the income at issue was generated by intangible trust assets whose only established link to Missouri is that the trust is administered there. While this connection with Missouri may be enough for Missouri to constitutionally tax this income, it does not rise to the level set forth in the regulation. Because we find former regulation 20 NYCRR 121.4(d) to be an appropriate interpretation of the legislative intent of section 620(a), we hold that the trust income was not "derived" from Missouri within the meaning of section 620.

In support of her position, petitioner cites Matter of Smith v. New York State Tax Commn. (120 AD2d 907, 503 NYS2d 169). In Smith, a Massachusetts trust paid fiduciary taxes to Massachusetts prior to making an accumulations distribution to Mrs. Smith, a New York resident and beneficiary of the trust. The Division argued that Mrs. Smith was not entitled to a resident tax credit because the Massachusetts tax was paid by the trust and not by Mrs. Smith. The Appellate Division, Third Department granted the credit. The Court found that because the petitioner was required to include in New York income both the amount of the actual distribution and the amount of the fiduciary tax paid by the trust, they effectively bore the burden of paying the Massachusetts tax (Matter of Smith v. New York State Tax Commn., *supra*, 503 NYS2d 169, 171). Thus, it found this result inconsistent with the legislative purpose of the section 620 credit -- to avoid double taxation on the same income. However, neither the decision of the Appellate Division nor the decision of the State Tax Commission reveal the nature of the income-producing assets and/or the manner in which the income was generated. Because this fact is critical in determining where income is "derived" from for purposes of section 620, the Smith decision does not control here (see, Matter of Leach v. Chu, *supra*). Further, the Leach decision

makes it clear that not all double taxation is avoided by the section 620 credit (Matter of Leach v. Chu, supra).

We agree with the Administrative Law Judge that the former State Tax Commission decisions cited by petitioner are not persuasive. In Matter of Myers (State Tax Commn., August 26, 1977), the petitioner was a New York resident who claimed the credit under section 620 for taxes paid to Pennsylvania on interest income from bank deposits and income from a trust fund held in Pennsylvania. The Commission upheld the denial of the credit for the interest income, but granted the credit for tax paid on income from the trust. However, the Commission failed to provide a statutory citation or its underlying rationale for granting the credit. Petitioner contends that it is reasonable to conclude that in granting the credit, the Commission interpreted the "business, trade or profession" language in former 20 NYCRR 121.4(d) to encompass income from a nonresident trust. It is critical to note that, as in Smith, the Myers decision does not indicate the nature of the assets comprising the trust corpus. We agree with the Administrative Law Judge that, without this critical fact, combined with the lack of legal analysis, the Myers decision is not controlling.

In Matter of Stover (State Tax Commn., June 13, 1983), a New York resident claimed a tax credit for "Minimum Tax" paid to Minnesota on income from two Minnesota trusts. The trusts owned marketable securities and real property in Minnesota which was leased to a mining company. The facts of the case indicate that "[e]ach trust receive[d] its income primarily from royalties arising from the shipments of taconite under a lease to the Taconite Company" (Matter of Stover, supra). In granting the credit, the Commission stated:

"the income consisting of royalties from the sale of taconite ore in the State of Minnesota . . . was 'income derived from sources within the other taxing jurisdiction' within the meaning and intent of section 620(a)" (Matter of Stover, supra).

The Commission did not make a separate finding as to the amount of income earned on the marketable securities, nor did it explain the manner in which the Minnesota Minimum Tax was calculated.

Petitioner contends that there is no reason to believe that Minnesota did not exercise its right to tax the income from marketable securities. Therefore, she argues, Stover holds that the resident tax credit is allowable with respect to intangibles held by a resident trust. However, because the facts in Stover do not describe how the Minnesota Minimum Tax was calculated, we decline to presume that the calculation included trust income derived from marketable securities.

Finally, petitioner argues that disallowance of the credit would violate the Commerce Clause of the United States Constitution, as it would result in a commercial advantage to trust administrators located in New York over those competing outside of New York -- namely, the avoidance of double taxation by New York resident beneficiaries on the income earned by New York trusts. The Administrative Law Judge rejected this argument, stating that the commercial advantage complained of is merely speculative. In response, petitioner, on exception, offers the following example: if the trusts at issue were located in New York, this would result in taxation of the trust income only by New York. Thus, according to petitioner, an incentive is provided to New York residents to establish a trust in New York as opposed to outside of New York. The result complained of results from the fact, as stated earlier, that two states with sufficient contacts with a taxpayer or his property may both constitutionally tax certain property or income of that taxpayer (Curry v. McCanless, *supra*). This is in stark contrast to the tax schemes held unconstitutional in Boston Stock Exch. v. State Tax Commn. (429 US 318) and in Westinghouse Elec. Corp. v. Tully (466 US 388), which provided a direct commercial advantage to local businesses. Therefore, we find these cases inapplicable to the instant situation.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Jane A. Mallinckrodt is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Jane A. Mallinckrodt is denied; and

4. The Notice of Deficiency dated August 11, 1987 is sustained.

DATED: Troy, New York
November 12, 1992

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner

/s/Maria T. Jones
Maria T. Jones
Commissioner