STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition of **LEONARD A. BLUE** for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Year 1981.	:	
In the Matter of the Petition of **LEONARD A. BLUE AND HELEN J. BLUE (DEC'D)** for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Years 1978 through 1980.	:	DECISION DTA NOS. 809244, 809245 AND 809246
In the Matter of the Petition of **LEONARD A. BLUE AND HARRIET D. BLUE** for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Years 1982 through 1984.	:	

Petitioners Leonard A. Blue, Leonard A. Blue and Helen J. Blue (Dec'd) and Leonard A. Blue and Harriet D. Blue, 2411 Rogue Valley Manor Drive, Medford, Oregon 97504, and the Division of Taxation each filed an exception to the determination of the Administrative Law Judge issued on April 21, 1994 with respect to petitioners' petitions. Petitioners appeared by Kelley, Drye & Warren (Martin B. Miller, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Michael J. Glannon, Esq., of counsel).

Petitioners and the Division of Taxation each submitted a brief in support of their exception and in opposition to the other party's exception. In addition, the Division submitted a reply brief. Petitioners had until November 9, 1994 to submit a reply brief, which date began thesix-month period for the issuance of this decision. Oral argument was not requested.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUES

I. Whether the retirement benefits received by petitioner Leonard A. Blue during the years in issue constituted a taxable annuity.

II. If the retirement benefits are determined to be taxable, whether, for tax years 1982, 1983 and 1984, petitioner Leonard A. Blue is entitled to a $20,000.00 reduction from Federal adjusted gross income under Tax Law § 612(c)(3-a).

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "3," "4" and "5" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

Prior to the years in issue, petitioner Leonard A. Blue[1] was a partner in the law firm of Kelley, Drye & Warren (the "Firm") which had offices within and without New York State. Mr. Blue was born on April 25, 1907 and was admitted to the New York State bar in 1932. He joined the Firm as an associate in September 1930 and became a partner of the Firm in January 1951. On January 1, 1977, Mr. Blue retired from the Firm, became a "life partner" pursuant to the Firm's written partnership agreement and, during the years at issue, was a nonresident of New York.

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[1]Petitioner Leonard Blue (in order to correspond to his Federal filings) filed joint returns for 1978 through 1980 with his then wife, Helen J. Blue, since deceased; an individual return for 1981; and joint returns for 1982 through 1984 with his present wife, Harriet D. Blue. Separate petitions were filed for each of these periods. Mr. Blue is being referred to as "petitioner" herein since the issues relate to certain payments received by Mr. Blue.

At the time Mr. Blue became a life partner, his capital account in the Firm was returned to him. Following his retirement, Mr. Blue did not perform any services for the Firm.

We modify finding of fact "3" of the Administrative Law Judge's determination to read as follows:

> Under the Life Partner Payment Provisions, Article Eighth, of the Firm partnership agreement in effect as of January 1, 1978 (the terms of which were the same as
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> parallel provisions in the Firm partnership agreement in effect as of petitioner's retirement on January 1, 1977), it was provided that a life partner would in general receive monthly each year from 1978 through 1982 one-twelfth of the greater of two annual amounts calculated for that year. Since petitioner's highest profit distribution percentage since January 1, 1970 was between 4.61 and 4.90, the two alternative amounts were (a) $36,000.00 plus $500.00 for each full 5% of the excess of the "Consumer Price Index for Urban Wage Earners and Clerical Workers - All Items" (the "CPI") for December of the preceding year over such index for 1972 (which was 127.3), and (b) $46,000.00. Life partner payments were subject to reduction in the event that (i) the total payments to life partners, as well as certain payments to the successor(s) in interest of deceased life partners, exceeded 20% of the Firm's profits for the year, or (ii) if paying the full annual payments to all life partners would result in certain partners being allocated Firm profits less than the highest unreduced life partner payment.[2]
>
> Article Third of the agreement stated that the profits and losses of the partnership would be distributed according to the Profit Distribution Percentage.
>
> The agreement provided at Article Eighth that a Life Partner did not have a Profit Distribution Percentage. Article Third of the agreement stated that "[a]ny partner who at the time does not have a Profit Distribution Percentage shall have no responsibility for the debts and liabilities of the partnership, and shall have no interest in the partnership assets or property." Article Eighth of the agreement provided for a four-year transition period from partner to a life partner, with the gradual elimination of the partner's Profit Distribution Percentage over the transition period. Article Fourth of the agreement provided that the reduction in a partner's Profit Distribution Percentage would result in a withdrawal from capital and a payment to the partner in an amount equal to the decrease in the partner's capital account.[3]

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[2] Article Eighth of Articles of Partnership, made as of January 1, 1978, is set forth in Appendix A.

[3] We modified the Administrative Law Judge's finding of fact "3" by adding the last two paragraphs to reflect more details of the record.

We modify finding of fact "4" of the Administrative Law Judge's determination to read as follows:

> The Firm's partnership agreement was restated and reexecuted in 1979; however, the operative provisions concerning life partner payments were unchanged.[4] In addition, the provisions stated above in paragraphs 2 and 3 of finding of fact "3" remained the same.[5]

We modify finding of fact "5" of the Administrative Law Judge's determination to read as follows:

> The Firm's partnership agreement was amended and restated as of January 1, 1980 and included changes in the provisions relating to life partners. In the case of petitioner, the partnership agreement contained separate provisions for the years 1980 through 1982 and for years beginning with 1983. For 1980 through 1982, petitioner's annual life partner payments were fixed by the partnership agreement at $56,000.00. For the years 1983 and 1984, petitioner's annual life partner payments were fixed at 115% of the "Basic Annual Life Payment" determined under the Firm's partnership agreement. According to the partnership provisions, the Basic Annual Life Payment for each year was $50,000.00 times a fraction, the numerator of which was 222.4 (the amount of the Consumer Price Index for Urban Wage Earners and Clerical Workers -- All Items: New York, N.Y. -- Northeastern, N.J. [the "Index"] for December 1979) plus or minus 75% of the amount of the increase or decrease in the Index between December 1979 and the completed calendar month immediately preceding such year, and the denominator of which was 222.4, subject to the following limitations:
>
> > "(1) The Basic Annual Life Partner Payment would not be reduced below $50,000;
> >
> > "(2) The Basic Annual Life Partner Payment would not be increased for any year so as to cause the percentage of annual increase in Basic Annual Life
> >
> > Payment for that year to exceed the percentage of annual increase in Average Partner Net Earnings for the immediately preceding year; and
> >
> > "(3) The Basic Annual Life Partner Payment would not be increased for any year so as to exceed 26% of Average Partner Net Earnings for the immediately preceding year."

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[4] Article Eighth of Articles of Partnership, made as of January 1, 1979, is set forth in Appendix B.

[5] We modified the Administrative Law Judge's finding of fact "4" by adding the second sentence to reflect more details of the record.

The Firm partnership agreement, effective as of January 1, 1980, provided for potential reductions in a life partner payment if it would exceed 50% of average partner earnings for such year, or if aggregate life partner payments would exceed 15% of Firm earnings for such year.[6] According to the affidavit of Thomas Carty, Director of Finance of the Firm, petitioner's 1980 through 1984 life partner payments were not limited by either of these limitations.

At Article Four, the 1980 agreement stated that:

> "Each Partner shall have an interest in the Partnership's capital in proportion to the Partner's Earnings Allocation Percentage. Partners without Earnings Allocation Percentages shall have no interest in the Partnership's capital."

Section 403 of the agreement provided that the Partnership Net Earnings and losses of the partnership would be allocated among the partners according to their Earnings Allocation Percentage.

Section 504 set forth the formula for eliminating a Life Partner's Earnings Allocation Percentage over a four-year transition period.[7]

Petitioner Leonard Blue received the following life partner payments pursuant to the agreements for the years in issue:

Year	Life Partner Payment, as Fixed by the Firm's Partnership Agreement
1978	$46,000.00
1979	46,000.00
1980	56,000.00
1981	56,000.00
1982	56,000.00
1983	57,500.00
1984	57,500.00

In March 1985, the New York State Department of Taxation and Finance, Revenue Opportunity Division, contacted petitioner regarding his nonfiling of New York State nonresident income tax returns for the taxable years 1978 through 1983.

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[6] Pertinent portions of partnership agreement as of January 1, 1980 are set forth in Appendix C along with the Tenth Supplement dated as of January 1, 1984.

[7] We modified the Administrative Law Judge's finding of fact "5" by adding the last three paragraphs to reflect more details of the record.

On December 12, 1985, petitioner filed New York State nonresident personal income tax returns (Form IT-203) for the taxable years 1978 through 1984, "paying the following amounts of tax and interest, while reserving all rights to claim a refund of the sums paid":

Year	Tax	Interest	Total
1978	$ 4,161.80	$ 3,419.77	$ 7,581.57
1979	3,632.00	2,597.84	6,229.84
1980	4,273.00	2,601.68	6,874.68
1981	3,768.00	1,721.48	5,489.48
1982	3,475.00	1,024.48	4,499.48
1983	3,333.00	605.10	3,938.10
1984	3,776.00	261.01	4,037.01
Total	$26,418.80	$12,231.36	$38,650.16

Accompanying the tax returns was a cover letter dated December 12, 1985 from Barry L. Salkin of the Firm. In this letter, Mr. Salkin outlined the historical background and legal position for petitioner's non-filing of the nonresident income tax returns. Mr. Salkin went on to state:

> "[H]owever, because of the hazards of litigation and certain proposed changes in the federal income tax law, taxpayer has determined to file New York State Nonresident Personal Income Tax Returns at this time, pending the outcome in the Pidot appeal. Of course, in the event that Pidot is reversed, and either the State Tax Commission elects not to appeal, or Pidot, as reversed by the Appellate Division, is affirmed by the Court of Appeals, or in the event of some other favorable development, taxpayer will file a Claim for Refund for each of the years in question."

Subsequent to the decision in Pidot v. State Tax Commn. (118 AD2d 915, 499 NYS2d 482, affd 69 NY2d 837, 513 NYS2d 965), petitioner, on December 4, 1987, filed amended returns for the taxable years 1978 through 1986, inclusive, treating the annuity payments as nontaxable pursuant to 20 NYCRR 131.4(d) and claiming refunds of all tax and interest paid with the original returns.

Sometime in early 1988, petitioner received a notice stating that the refund claim for 1984 would have to be processed by hand. By November 1, 1989, petitioner had received neither a refund nor a notice of disallowance of the claimed refunds. Petitioner submitted a request for a conciliation conference on November 1, 1989.

On June 8, 1990, petitioner received a "Notice of Disallowance" from the Audit Division, Central Income Tax Section ("Division"), which disallowed petitioner's claim for tax years 1978 through 1984. The reason for the disallowance was as follows:

> "[U]pon review of the information received from the partnership, Coopers and Lybrand [sic], concerning payments made to retired partners, it has been determined that the payments received by you from the partnership as a retired partner do not qualify as an annuity under Regulation Section 131.4(d) for the reason that a restrictive covenant condition exists. A qualified annuity entails the payment of a definite sum of money without contingency."

Conciliation conferences for tax years 1978 through 1980, 1981, and 1982 through 1984 were held on August 9, 1990. In three separate conciliation orders, dated November 23, 1990, the conferee denied the refund claims for the tax years 1978 through 1980, 1981, and 1982 through 1984.

Petitioner filed three separate petitions, dated February 19, 1991, which requested refund of the nonresident personal income taxes paid for tax years 1978 through 1984, inclusive, plus interest.

Three answers, each dated July 3, 1991, were filed by the Division.

OPINION

Tax Law former § 632(a)(1)(A) provided:

> "The New York adjusted gross income of a nonresident individual shall be the sum of the following:
>
> "(1) The net amount of items of income, gain, loss and deduction entering into his federal adjusted gross income, as defined in the laws of the United States for the taxable year, derived from or connected with New York sources, including:
>
> "(A) his distributive share of partnership income, gain, loss and deduction, determined under section six hundred thirty-seven . . . ."

The Administrative Law Judge concluded that Mr. Blue did receive a distributive share of partnership income for the years in issue which was properly includable in petitioner's New York adjusted gross income under Tax Law former § 632(a)(1)(A). This conclusion of the Administrative Law Judge was based on the facts that:

> "[f]or tax years 1978 and 1979, life partner payments were paid out of the Firm's partnership profits. In addition, determination of a life

> partner's 'stipulated annual amount' was based upon that particular life partner's highest profit distribution percentage since January 1, 1970. [footnote omitted] For tax years 1980 through 1984, each life partner received an 'annual life partner payment' in 12 equal installments, which was paid out of partnership earnings. [footnote omitted] Under the terms of the 1980 partnership agreement, a life partner's earnings allocation percentage was utilized in the calculation to determine the annual life partner payment which he received" (Determination, conclusion of law "E").

We conclude that the Administrative Law Judge erred in this holding.

Together Matter of Pidot v. State Tax Commn. (supra) and Matter of Kestenbaum v. State Tax Commn. (107 AD2d 955, 484 NYS2d 371) establish that the meaning of "distributive share" for purposes of Tax Law former § 632(a)(1)(A) is determined by the meaning of this phrase in sections 704(a) and 736(a) of the Internal Revenue Code. Under section 704(a) of the Code, the Court in each case held, that a partner's distributive share is determined by the partnership agreement. If the agreement gives the taxpayer no interest in the partnership's income or losses and distributes 100% of income and losses to individuals other than the taxpayer, then the Court concluded the taxpayer has no interest in the partnership and did not receive a distributive share under section 704(a) of the Internal Revenue Code. Further, the Court in Kestenbaum and Pidot held that payments were not a distributive share under section 736 of the Code, if the payments were made after the taxpayer's interest in the partnership had already been completely liquidated.

We find the facts of this case to be indistinguishable from those in Kestenbaum and Pidot and, therefore, conclude that the payments to Mr. Blue were not a distributive share of partnership income. Mr. Blue, like the petitioners in Kestenbaum and Pidot, had no right to share, under the terms of the relevant agreements, in the profits or losses of the partnership and this right was given 100% to others who had either a Profit Distribution Percentage or, for the years 1980 through 1984, an Earnings Allocation Percentage. Further, Mr. Blue, also like the petitioner in Kestenbaum and Pidot, had retired from the partnership prior to the years at issue and his interest in the partnership had been completely liquidated at the time that he became a Life Partner. Thus, we must conclude that the payments to Mr. Blue were not a distributive

share under either section 704(a) or 736 of the Internal Revenue Code nor, therefore, under Tax Law former § 632(a)(1)(A).

The Administrative Law Judge also stated that "[b]ecause the retirement payments paid to petitioner by the Firm were attributable to services he rendered in New York prior to his retirement in 1977, these payments constituted income attributable to a business, trade, profession or occupation carried on in New York State (see, Tax Law former § 632[a],[b][1][B]; 20 NYCRR former 131.4[d])" (Determination, conclusion of law "E"). We believe that this is a separate, independent basis upon which to tax the income at issue and we affirm the Administrative Law Judge's determination on this basis.

Tax Law former § 632(b)(1)(B) provides as follows:

> "Income and deductions from New York sources.
>
> "(1) Items of income, gain, loss and deduction derived from or connected with New York sources shall be those items attributable to:
>
> * * *
>
> "(B) a business, trade, profession or occupation carried on in this state."

Although petitioners have argued that the income at issue was not a distributive share of partnership income, they have provided little evidence as to what the income was.[8] We conclude from the record before us that the payments were in consideration of services rendered to the partnership prior to Mr. Blue's retirement. In Matter of Walsh (Tax Appeals Tribunal, November 19, 1992, affd on other grounds Matter of Walsh v. Tax Appeals Tribunal, 196 AD2d 367, 609 NYS2d 405), we concluded that "the words 'derived from or connected with New York sources' require an examination of the nonresident's activities from which the income was secured or earned, not when the benefit was received or realized [citations omitted]." On this basis, we concluded in Walsh that payments from a New York partnership to a retired nonresident partner were derived from or connected with New York sources within the meaning

[8]In their legal argument with respect to the second issue before us, whether the payments constitute an annuity, petitioners acknowledge that the payments were a pension or other retirement benefit related to Mr. Blue's prior services to the firm.

of former section 632(b)(1)(B). We can see no reason why the same result should not apply here.

We believe that the Court of Appeals decision in Matter of Michaelsen v. New York State Tax Commn. (67 NY2d 579, 505 NYS2d 585) supports our conclusion here and in Walsh. In Michaelsen, the Court held that a portion of the income generated from stock options received as a result of New York employment retained its character as income derived from or connected with New York sources even though the nonresident taxpayer did not recognize the income from the options until much later when the stock was sold. We can think of no reason why a former partner should be treated differently from an employee under former section 632(b)(1)(B) (see, Matter of Norris v. State Tax Commn., 140 AD2d 876, 528 NYS2d 694).

Our conclusion that the income at issue is includable in petitioners' New York adjusted gross income pursuant to former section 632(b)(1)(B) is not inconsistent with the Courts' decisions in Kestenbaum and Pidot. In each case, the Court explicitly stated that it could not uphold the State Tax Commission's determination on a basis not stated in the determination. In each of the underlying State Tax Commission decisions, only former sections 632(a)(1)(A) and 637 were relied on. Neither determination mentioned former section 632(b)(1)(B).

We must next determine if the payments at issue were excludable from petitioners' New York income under former 20 NYCRR 131.4(d). This regulation provides as follows:

> "(1) General. Where an individual formerly employed in New York State is retired from service and thereafter receives a pension or other retirement benefit attributable to his former services, the pension or retirement benefit is not taxable for New York State personal income tax purposes if the individual receiving it is a nonresident and if it constitutes an annuity as defined in paragraph (2) of this subdivision. Where a pension or other retirement benefit does not constitute an annuity, it is compensation for personal services and, if the individual receiving it is a nonresident, it is taxable for New York State personal income tax purposes to the extent that the services were performed in New York State . . . .
>
> "(2) Definition. To qualify as an annuity, a pension or other retirement benefit must meet the following requirements.
>
> "(i) It must be paid in money only, not in securities of the employer or other property.

"(ii) It must be payable at regular intervals, at least annually, for the life of the individual receiving it, or over a period not less than half his life expectancy, as of the date payments begin . . . .

"(iii) It must be payable:

"(a) at a rate which remains uniform during such life or period; or

"(b) at a rate which varies only with:

"(1) the fluctuation in the market value of the assets from which such benefits are payable;

"(2) the fluctuation in a specified and generally recognized cost-of-living index; or

"(3) the commencement of social security benefits; or

"(c) in such a manner that the total of the amounts payable is determinable at the annuity starting date either directly from the terms of the contract or indirectly by the use of either mortality tables or compound interest computations, or both, in conjunction with such terms and in accordance with sound actuarial theory. The term annuity starting date in the case of any contract or plan is the first day of the first period for which an amount is received as an annuity by the individual under the contract or plan.

"(iv) The individual's right to receive it must be evidenced by a written instrument executed by his employer, or by a plan established and maintained by the employer in the form of a definite written program communicated to his employees" (20 NYCRR former 131.4[d]).

The Administrative Law Judge held that the payments did not satisfy the uniformity requirement of 20 NYCRR former 131.4(d)(2)(iii). The payments pursuant to the 1978 and 1979 agreements did not satisfy this requirement, the Administrative Law Judge concluded, because under Article Eighth (b),

"the stipulated annual amounts payable to a life partner would be reduced proportionately to the extent they and 'the minimum required payments to the successor or successors in interest of deceased Life Partners' exceed 20% of the profits of the partnership for that year. There would also be a reduction in all of the stipulated life partner amounts if a partner was to receive an amount less than the highest

> stipulated annual life partner amount" (Determination, conclusion of law "F").

The payments for 1980 through 1984 did not satisfy the uniformity requirement of 20 NYCRR former 131.4(d)(2)(iii), the Administrative Law Judge concluded, because under section 502(b) of the 1980 agreement,

> "annual life partner payments would be reduced proportionately if annual life partner payments were to exceed 15% of parntership earnings in any fiscal year. . . . For the years 1983 and 1984, under the terms of Section 502(c), the annual adjustment to the 'basic annual life partner payment' could have been and sometimes was limited by 'average partner net earnings' for the previous year" (Determination, conclusion of law "F").

The Administrative Law Judge determined that these provisions meant that Mr. Blue's life partner payments "depended upon and varied with the law firm profits for the year or average partner net earnings for the previous year" (Determination, conclusion of law "F") and that under Matter of Norris v. State Tax Commn. (supra) and Matter of Walsh (supra) this type of variation was not authorized by the regulation.

On exception, petitioner argues that:

> "[w]hile the Firm partnership agreement certain [sic] potential limitations on Life Partner Payments determined pursuant to the formulae set out in the agreement and discussed in the Statement of Facts . . . these limitations never applied to Petitioner or any other Life Partner for the years in question. Thus, these limitations on Petitioner's Life Partner Payments, which otherwise qualify as nontaxable annuities, should be disregarded in determining whether Petitioner's Life Partner Payments constituted an annuity under former 20 NYCRR 131.4(d)" (Petitioner's brief on exception, p. 14).

We believe that the Administrative Law Judge correctly and adequately addressed this issue and we affirm her determination on this issue for the reasons stated in the determination.

The next issues before us are those raised by the Division in its exception.

The Administrative Law Judge allowed petitioners to amend their claim for a refund to add the alternative ground that they were entitled to the $20,000.00 subtraction modification provided by Tax Law § 612(c)(3-a). Relying on St. Joseph Lead Co. v. United States (299 F2d 348, 62-1 USTC ¶ 9278), the Administrative Law Judge allowed the amendment because the $20,000.00 subtraction modification was an alternative ground for an existing timely filed claim

and "[t]he determination of whether the retirement benefits were taxable has a direct bearing on whether a Tax Law § 612(c)(3-a) subtraction modification would be necessary. The only additional fact which the Division would need to determine whether petitioners were entitled to the . . . subtraction modification for tax years 1982, 1983 and 1984 was Mr. Blue's age" (Determination, conclusion of law "H").

The Division argues that the bases of the two refund claims were totally unrelated and, therefore, the present circumstances are totally unlike that in St. Joseph Lead.

We affirm the determination of the Administrative Law Judge on this issue for the reasons stated in her determination.

Lastly, the Division challenges the Administrative Law Judge's conclusion that petitioners were entitled to the section 612(c)(3-a) subtraction modification.

Section 612(c)(3-a) provides as follows:

> "(c) Modifications reducing federal adjusted gross income. There shall be subtracted from federal adjusted gross income:
>
> * * *
>
> "(3-a) Pensions and annuities received by an individual who has attained the age of fifty-nine and one-half . . . to the extent includible in gross income for federal income tax purposes, but not in excess of twenty thousand dollars, which are periodic payments attributable to personal services performed by such individual prior to his retirement from employment, which arise (i) from an employer-employee relationship or (ii) from contributions to a retirement plan which are deductible for federal income tax purposes . . . ."

The Administrative Law Judge reasoned that section 612(c)(3-a) is in many respects similar to 20 NYCRR former 131.4(d) and that the Court in Pidot concluded that the regulation should apply to partners as well as employees. Therefore, the Administrative Law Judge concluded that section 612(c)(3-a) should apply to partners as well as employees.

On its face, section 612(c)(3-a) requires that the payments arise either from an employer-employee relationship or from contributions to a retirement plan deductible for Federal income tax purposes. Petitioners allege that they satisfy the former because the Legislature intended

employee to include partner. Petitioners assert that this legislative intent is evidenced by the fact that in other sections of section 612 (specifically, section 612[o][1][B][iii] and 612[p][5]) employee does include partners. In our view, the sections to which petitioners refer evidence only an excess of caution in legislative drafting intended to ensure that "employees" in those particular provisions not be interpreted to mean partners and does not evidence that the Legislature generally meant employee to mean partner.

A partnership is defined as "an association of two or more persons to carry on as co-owners a business for profit" (Partnership Law, § 10). The partners have a fiduciary relationship to each other (Partnership Law, § 43[1]). The hallmark of an employer-employee relationship is that the employer has reserved the right of control over the manner in which the employee performs the employer's work (Matter of Villa Maria Inst. of Music v. Ross, 54 NY2d 691, 442 NYS2d 972). This right of control is inconsistent with the relationship between partners which is based on the concept of co-ownership and an equal responsibility (see, Hill v. Curtis, 154 App Div 662, 139 NYS 428). Given these basic differences, we conclude that the Legislature did not intend "employee" to include a partner for purposes of the section 612(c)(3-a) subtraction modification and, therefore, that the income at issue cannot be excluded from petitioners' New York income on this basis.

As suggested by the above, we think that the Administrative Law Judge erred in analogizing the instant question to former 20 NYCRR 131.4(d) and in relying on the Court of Appeals' decision in Pidot. The Court in Pidot explicitly held that the Division's interpretation of 20 NYCRR former 131.4(d) as applying only to employees had no basis in the relevant statutory language and, therefore, could not be sustained. In contrast, here the relevant statutory language is explicitly limited to employees.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Leonard A. Blue, Leonard A. Blue and Helen J. Blue (Dec'd) and Leonard A. Blue and Harriet D. Blue is denied;

2. The exception of the Division of Taxation is granted to the extent that it is held that petitioners Leonard A. Blue and Harriet D. Blue are not entitled to the subtraction modification of section 612(c)(3-a) of the Tax Law, but the exception is otherwise denied;

3. The determination of the Administrative Law Judge is modified to the extent indicated in paragraph "2" above, but the determination is otherwise sustained; and

4. The petitions and claims for refund of Leonard A. Blue, Leonard A. Blue and Helen J. Blue (Dec'd) and Leonard A. Blue and Harriet D. Blue are denied.

DATED: Troy, New York
April 6, 1995

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

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

APPENDIX A

"Articles of Partnership, made as of January 1, 1978.

"ARTICLE EIGHTH

"Life Partner

* * *

"Messrs. Blue . . . became Life Partners on January 1, 1977 and shall be entitled to the amount provided in this Article Eighth.

"During each year, a Life Partner shall have no Profit Distribution Percentage but there shall be paid to him out of the profits of the partnership each month until his death one-twelfth (1/12) of the annual amount provided for in paragraph (a) or (b), whichever is greater.

(a)

"The stipulated amount determined from the following table after making the adjustment set forth in the paragraph following the table:

Highest Profit Distribution Percentage since January 1, 1970	Stipulated Annual Amount
4.0 or lower	$30,000
4.01 to 4.30	32,000
4.31 to 4.60	34,000
4.61 to 4.90	36,000
4.91 to 5.20	38,000
5.21 or higher	40,000

"For each of the years 1978 through 1982 the 'Adjustment Years'), if the 'Consumer Price Index for Urban Wage Earners and Clerical Workers - All Items' of the United States Bureau of Labor Statistics for the month of December preceding each such Adjustment Year exceeds by 5% or more such Index for the month of December, 1972, there will be added to the stipulated annual amount for the Adjustment Year following such December $500 for each full 5% of such excess. The implementation of such adjustments will be subject to reevaluation in the light of the amounts the partners who are not Life Partners receive from the profits of the partnership. Subsequent to the year 1982, and at three year intervals thereafter a review will be

made of the aforesaid Index and the amounts the partners who are not Life Partners receive from the profits of the partnership to see whether additional adjustments would be equitable.

(b)

"The stipulated amount determined from the following table:

Highest Profit Distribution Percentage since January 1, 1970	Stipulated Annual Amount
4.0 or lower	$40,000
4.01 to 4.30	42,000
4.31 to 4.60	44,000
4.61 to 4.90	46,000
4.91 to 5.20	48,000
5.21 or higher	50,000

"The stipulated annual amounts, payable pursuant to paragraph (a) and (b), as otherwise adjusted for any year, shall be reduced proportionately to the extent they and the minimum required payments to the successor or successors in interest of deceased Life Partners pursuant to Article Ninth exceed twenty per cent (20%) of the profits of the partnership for such year. In addition, if in any year any partner who graduated from law school at least eight years prior to the beginning of such year and who is not a Life Partner nor in his Transition Period would receive (after giving effect to the preceding sentence but before giving effect to this sentence) from the profits of the partnership less than the highest level of stipulated annual amounts as otherwise adjusted which any Life Partner would receive for such year, the stipulated annual amounts payable to all Life Partners for such year shall be reduced as follows: the highest level of stipulated annual amounts as otherwise adjusted which any Life Partner would receive for such year shall be reduced algebraically to an amount equal to the smallest share of the partnership profits to be received after giving effect to this sentence by a partner who graduated from law school at least eight years prior to the beginning of such year and who is not a Life Partner nor in his Transition Period, and the remaining levels of stipulated annual amounts as otherwise adjusted shall be reduced in the same proportion. Any reductions required by the provisions of this paragraph may be made by reducing the payments to be made in the balance of the year involved or in any succeeding year, by reducing the payments to be made under

Articles Seventh or Ninth, or by any combination thereof, and to the extent not so recovered shall be repayable to the partnership by the Life Partner or his personal representatives.

"Each Life Partner may continue to be as active in the practice of the partnership as he prefers to be and will be provided with office space and other services appropriate to the degree of his activity in the partnership's practice. All compensation for services and advice of a Life Partner shall continue to be partnership income in the same manner and to the same extent as prior to his becoming a Life Partner, and the provisions of Article Seventh with respect to Ancillary Income shall continue to apply to him.

* * *

"The provisions of this Article Eighth with respect to reduction of Profit Distribution Percentages during the Transition Period, the minimum amount payable to a partner during any year of his Transition Period, and the stipulated annual amounts and adjustments thereto for Life Partners shall govern the Profit Distribution List in force at any time, and such provisions of this Article Eighth shall become operative automatically. Each Profit Distribution List shall be subject to the provisions of this paragraph."

APPENDIX B

"Articles of Partnership, made as of January 1, 1979

"ARTICLE EIGHTH

"Life Partner

* * *

"Messrs. Blue . . . became Life Partners on January 1, 1977 and shall be entitled to the amount provided in this Article Eighth.

"During each year, a Life Partner shall have no Profit Distribution Percentage but there shall be paid to him out of the profits of the partnership each month until his death one-twelfth (1/12) of the annual amount provided for in paragraph (a) or (b), whichever is greater.

(a)

"The stipulated amount determined from the following table after making the adjustment set forth in the paragraph following the table:

Highest Profit Distribution Percentage since January 1, 1970	Stipulated Annual Amount
4.0 or lower	$30,000
4.01 to 4.30	32,000
4.31 to 4.60	34,000
4.61 to 4.90	36,000
4.91 to 5.20	38,000
5.21 or higher	40,000

"For each of the years 1979 through 1982 the 'Adjustment Years'), if the 'Consumer Price Index for Urban Wage Earners and Clerical Workers - All Items' of the United States Bureau of Labor Statistics for the month of December preceding each such Adjustment Year exceeds by 5% or more such Index for the month of December, 1972, there will be added to the stipulated annual amount for the Adjustment Year following such December $500 for each full 5% of such excess. The implementation of such adjustments will be subject to reevaluation in the light of the amounts the partners who are not Life Partners receive from the profits of the partnership. Subsequent to the year 1982, and at three year intervals thereafter a review will be made of the aforesaid Index and the amounts the partners who are not Life Partners receive from the profits of the partnership to see whether additional adjustments would be equitable.

(b)

"The stipulated amount determined from the following table:

Highest Profit Distribution Percentage since January 1, 1970	Stipulated Annual Amount
4.0 or lower	$40,000
4.01 to 4.30	42,000
4.31 to 4.60	44,000
4.61 to 4.90	46,000
4.91 to 5.20	48,000
5.21 or higher	50,000

"The stipulated annual amounts, payable pursuant to paragraph (a) and (b), as otherwise adjusted for any year, shall be reduced proportionately to the extent they and the minimum

required payments to the successor or successors in interest of deceased Life Partners pursuant to Article Ninth exceed twenty per cent (20%) of the profits of the partnership for such year. In addition, if in any year any partner who graduated from law school at least eight years prior to the beginning of such year and who is not a Life Partner nor in his Transition Period would receive (after giving effect to the preceding sentence but before giving effect to this sentence) from the profits of the partnership less than the highest level of stipulated annual amounts as otherwise adjusted which any Life Partner would receive for such year, the stipulated annual amounts payable to all Life Partners for such year shall be reduced as follows: the highest level of stipulated annual amounts as otherwise adjusted which any Life Partner would receive for such year shall be reduced algebraically to an amount equal to the smallest share of the partnership profits to be received after giving effect to this sentence by a partner who graduated from law school at least eight years prior to the beginning of such year and who is not a Life Partner nor in his Transition Period, and the remaining levels of stipulated annual amounts as otherwise adjusted shall be reduced in the same proportion. Any reductions required by the provisions of this paragraph may be made by reducing the payments to be made in the balance of the year involved or in any succeeding year, by reducing the payments to be made under Articles Seventh or Ninth, or by any combination thereof, and to the extent not so recovered shall be repayable to the partnership by the Life Partner or his personal representatives.

"Each Life Partner may continue to be as active in the practice of the partnership as he prefers to be and will be provided with office space and other services appropriate to the degree of his activity in the partnership's practice. All compensation for services and advice of a Life Partner shall continue to be partnership income in the same manner and to the same extent as prior to his becoming a Life Partner, and the provisions of Article Seventh with respect to Ancillary Income shall continue to apply to him.

* * *

"The provisions of this Article Eighth with respect to reduction of Profit Distribution Percentages during the Transition Period, the minimum amount payable to a partner during any

year of his Transition Period, and the stipulated annual amounts and adjustments thereto for Life Partners shall govern the Profit Distribution List in force at any time, and such provisions of this Article Eighth shall become operative automatically. Each Profit Distribution List shall be subject to the provisions of this paragraph."

APPENDIX C

"Agreement, as of January 1, 1980

* * *

"ARTICLE ONE

"DEFINITIONS AND PROVISIONS OF GENERAL APPLICATION

"Section 101. Definitions.

* * *

"'Annual Life Partner Payment' has the meaning specified in Section 502 of this Agreement.

"'Average Partner Allocation Percentage' means for any Fiscal Year the percentage, rounded to the nearest one-hundredth of one percent, which is obtained when one hundred is divided by the total number of Partners provided with Earnings Allocation Percentages in the Earnings Allocation List for that Fiscal Year prior to any modifications required by paragraph (c) of Section 304 of this Agreement.

"'Average Partner Net Earnings' means for any Fiscal Year the amount obtained when Partnership Net Earnings for that Fiscal Year is divided by the number of Partners other than Life Partners in that Fiscal Year. For purposes of determining the number of Partners other than Life Partners in a Fiscal Year, a Partner who was a Partner for part of a Fiscal Year shall be counted by a fraction equal to the fraction of the Fiscal Year during which the Partner was a Partner.

"'Basic Annual Life Partner Payment' has the meaning specified in Section 502 of this Agreement.

* * *

"'Life Partner' has the meaning specified in Article Five of this Agreement and includes Retired Life Partner.

* * *

"'Partnership Distributable Net Earnings' means Partnership Net Earnings remaining after payment of all minimum amounts and all stipulated amounts, if any, provided in an Earnings Allocation List.

"'Partnership Earnings' means the Partnership Revenues remaining after payment of all the Partnership's expenses and charitable contributions.

* * *

"'Partnership Net Earnings' means the Partnership Earnings remaining after payment of all amounts paid to Life Partners pursuant to Section 502 of this Agreement and with respect to Former Partners pursuant to Section 604 of this Agreement.

* * *

"'Retired Life Partner' has the meaning specified in Section 505 of this Agreement.

* * *

"ARTICLE FIVE

"LIFE PARTNERSHIP

"Section 501. Life Partners.

"Except as otherwise provided in this Agreement, each Partner shall become a Life Partner upon the expiration of the Partner's Transition Period. Each Life Partner may continue to be as active in the practice of the Partnership as the Life Partner prefers and shall be provided with office space and other services appropriate to the degree of that activity.

"Section 502. Payments to Life Partners.

"(a) The Partnership shall pay each Life Partner an Annual Life Partner Payment in twelve equal installments on the first business day of each calendar month.

"(b) The Annual Life Partner Payment for each Life Partner shall be a percentage of the then effective Basic Annual Life Partner Payment based upon the greatest percentage rounded

to the nearest whole percent obtained when the Life Partner's Earnings Allocation Percentage for a Fiscal Year prior to any modifications required by paragraph (c) of Section 304 of this Agreement is divided by the Average Partner Allocation Percentage for that Fiscal Year in any one Fiscal Year from 1973 to 1979 inclusive or in at least three Fiscal Years after 1979 determined in accordance with the following table:

Greatest Percentage Obtained When A Partner's Earnings Allocation Percentage Is Divided By The Average Partner Allocation Percentage In Any One Fiscal Year From 1973 to 1979 Inclusive Or In At Least Three Fiscal Years After 1979		Percentage Of Basic Annual Life Partner Payment
Less than 110 Percent	-	100 Percent
110 Percent or More	-	105 Percent
120 Percent or More	-	110 Percent
130 Percent or More	-	115 Percent
140 Percent or More	-	120 Percent
150 Percent or More	-	125 Percent

"Annual Life Partner Payments shall be reduced proportionally so that the aggregate Annual Life Partner Payments in any Fiscal Year shall not exceed fifteen percent of Partnership Earnings for that Fiscal Year. In addition no Annual Life Partner Payment in any Fiscal Year shall exceed fifty percent of Average Partner Net Earnings in that Fiscal Year.

"(c) The Basic Annual Life Partner Payment for the Partnership's 1980, 1981 and 1982 Fiscal Years shall be $50,000. In each subsequent Fiscal Year the Basic Annual Life Partner Payment shall be the amount obtained when $50,000 is multiplied by a fraction of which the numerator is two hundred twenty two and four-tenths (222.4), which is the amount of the 'Consumer Price Index for Urban Wage Earners and Clerical Workers -- All Items: New York, N.Y. - Northeastern N.J.' of the United States Bureau of Labor Statistics for December 1979, plus or minus seventy five percent of the amount of the increase or decrease in the Index between December 1979 and the completed calendar month immediately preceding such subsequent Fiscal Year and the denominator is two hundred twenty two and four-tenths (222.4).

Each annual adjustment to Basic Annual Life Payment pursuant to the previous sentence shall be subject to the following limitations:

"(1) Basic Annual Life Partner Payment shall not be reduced below $50,000;

"(2) Basic Annual Life Partner Payment shall not be increased for any Fiscal Year so as to cause the percentage of annual increase in Basic Annual Life Payment for that Fiscal Year to exceed the percentage of annual increase in Average Partner Net Earnings for the immediately preceding Fiscal Year; and

"(3) Basic Annual Life Partner Payment shall not be increased for any Fiscal Year so as to exceed twenty six percent (26%) of Average Partner Net Earnings for the immediately preceding Fiscal Year.

"Partners having an aggregate Earnings Allocation Percentage in excess of fifty may at any time determine that future increases to the Basic Annual Life Partner Payment pursuant to this paragraph (c) shall be further limited or eliminated entirely but that determination shall not reduce the amount of Basic Annual Life Partner Payment then in effect.

* * *

"Section 705. Messrs. Blue, et al..

"(a) The dates on which Messrs. Blue . . . became or will become Life Partners, his Annual Life Partner Payment for Fiscal Years 1980, 1981 and 1982, if applicable, and the percentage of Basic Annual Life Partner Payment which determines his Annual Life Partner Payment for Fiscal Years after 1982 are set forth in the following table:

Partner	Commencement of Life Partnersrhip January 1,	Annual Life Partner Payment in 1980, 1981 and 1982 as Applicable	Percentage of Basic Annual Life Partner Payment After 1982
Mr. . . .	1981	$50,000	100 Percent
Mr. Blue	1977	$56,000	115 Percent
Mr. . . .	1982	$50,000	100 Percent
Mr. . . .	1977	$54,000	110 Percent
Mr. . . .	1979	$50,000	100 Percent
Mr. . . .	1977	$50,000	100 Percent
Mr. . . .	1982	$60,000	125 Percent
Mr. . . .	1977	$60,000	125 Percent

* * *

"Tenth Supplement
Dated as of January 1, 1984
to the Agreement
Made as of January 1, 1980
forming Kelley Drye & Warren

* * *

"Section 4. Paragraph (a) of Section 502. Payments to Life Partners. shall be amended to state in its entirety:

'(a) The Partnership shall pay each Life Partner an Annual Life Partner Payment in twelve equal installments on the first business day of each calendar month. There shall be deducted from a Life Partner's Annual Life Partner Payment an amount equal to the Partner Retirement Plan Contributions by the Partnership on behalf of that Life Partner.'"