STATE OF NEW YORK

DIVISION OF TAX APPEALS

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| In the Matter of the Petition | : | |
| of | : | |
| KENNETH J. CORT | : | DETERMINATION<br>DTA NO. 811179 |
| for Redetermination of a Deficiency or for Refund of New York State and New York City Income Taxes under Article 22 of the Tax Law and the New York City Administrative Code for the Years 1986 and 1987. | : | |

Petitioner, Kenneth J. Cort, 91 Meadow Ridge, Avon, Connecticut 06001, filed a petition for redetermination of a deficiency or for refund of New York State and New York City income taxes under Article 22 of the Tax Law and the New York City Administrative Code for the years 1986 and 1987.

A hearing was held before Marilyn Mann Faulkner, Administrative Law Judge, at the offices of the Division of Tax Appeals, Riverfront Professional Tower, 500 Federal Street, Troy, New York, on July 26, 1993 at 9:15 A.M., with all briefs due by December 1, 1993. Petitioner, represented by Goodkind, Labaton, Rudoff & Sucharow (Mark S. Arisohn, Esq., of counsel), filed a brief on October 5, 1993. The Division of Taxation, represented by William F. Collins, Esq. (Lawrence A. Newman, Esq., of counsel), filed a letter brief on October 20, 1993. Petitioner filed a reply brief on December 1, 1993.

ISSUES

I. Whether the Division of Taxation used the correct allocation ratios in determining a nonresident's New York State and City income tax for the years 1986 and 1987 based on services performed in New York for a Texas-based corporation.

II. Whether the sale of 24,000 shares of stock by a nonresident, who obtained the shares from his employer, a Texas-based corporation, as part of the company's executive stock plan, is subject to New York income tax as income "derived from or connected with New York

sources."

FINDINGS OF FACT

Petitioner, Kenneth J. Cort, began his career in the retail business in 1965 with the department store of Abraham & Strauss in New York City. In 1973 he was promoted to a vice-president position with Abraham & Strauss and moved from New York to a house in New Jersey.

In January of 1984, petitioner took a position as a high-level executive with Zale Corporation, which sold moderately priced fine jewelry at the retail level. Zale Corporation was located in Irving, Texas, a suburb of Dallas. Petitioner relocated to Texas from New Jersey and bought a home in Texas in July of 1984. Petitioner rented his New Jersey home until its sale in 1986.

Zale Corporation maintained a New York City office which occupied space of approximately 10,000 to 12,000 square feet. The New York office dealt with the procurement of raw materials and the transformation of raw materials into finished products.

Petitioner was responsible for sales and in 1984 spent a great deal of time developing an organizational structure for the company. As a result, petitioner spent less time travelling in 1984 than he did in subsequent years.

From the beginning of 1986 through the end of February of 1987, petitioner took frequent trips to New York City. Petitioner explained in his testimony that these trips were for both personal and business reasons. During 1986, Zale Corporation, which was a family business, was experiencing a possible hostile takeover. Therefore, as a senior executive, petitioner visited New York City periodically in 1986 and the beginning of 1987 to attend trade shows and to establish personal contacts with the corporation's suppliers to ensure a continued level of supplies by reassuring suppliers, in the face of takeover rumors, that the company was financially stable. Petitioner testified that the situation required more trips to New York than would have normally occurred. In addition, petitioner and his wife separated after their move to Texas. Petitioner's wife moved back to New York City and was living there during the time

period in question. Petitioner's children, ages 12 and 17 at that time, remained in Texas with him to attend school. Therefore, the business trips to New York were often combined with petitioner's desire to spend time with his wife to attempt a reconciliation. Petitioner testified that Zale Corporation was a family-oriented business that was very supportive of his attempts at reconciliation.[1] Petitioner also used these trips as opportunities to visit his daughter attending summer camp in upstate New York during July of 1986 and to spend a few days in August of 1986 to vacation at the Saratoga Race Track.

Petitioner and his wife filed joint New York State nonresident income tax returns for 1986 and 1987.

In 1989, the Division of Taxation ("Division") commenced a tax audit of petitioner and his wife.[2] After a full audit and analysis

of petitioner's diaries for 1986 and 1987, the auditor concluded that the following days were days that petitioner worked in his New York office:

1986 - Total 72 days

January 9-12
January 31
February 1-7
February 24-25
April 9-16
April 30
May 1-2
May 6-8
May 27-28
June 19-20
July 25 - August 4
September 9-13
September 25-29
October 22-25
November 3-12
December 10-13
December 29

1987 - Total 26 days

January 8-11
January 13-16
January 20
January 22

[1]Petitioner and his wife subsequently reconciled their marriage.

[2]Deficiencies found by the Division with respect to Mrs. Cort's income are not the subject of this petition.

January 27 - February 9
February 16
March 4

In her workpapers, the Division's auditor calculated the ratio of New York days to the total number of days worked in 1986 to be 27.9% (72 [New York days] divided by 258 [total workdays]) and multiplied that percentage by the 1986 income of $321,225.00 to arrive at New York income of $89,644.00 to which she applied a $42,595.00 partnership loss. Similarly, the auditor calculated the ratio in 1987 (through March 6, 1987) to be 57.77% (26 [New York days] divided by 45 [total workdays]).[3] The

auditor averaged the two ratios (42.83%) and then applied the 27.9% to 1987 New York wages of $391,689.00 for a total of $109,281.00 and applied the average ratio of 42.83% to New York benefits of $1,314,440.00 for a total of $562,975.00. At the hearing, the auditor, who testified on behalf of the Division,[4] explained that the calculation of the 1987 wages was an error in favor of the taxpayer because she applied the lower 1986 ratio to the 1987 wages. Thus, for 1987 the auditor calculated New York wages and benefits to be $109,281.00 and $562,975.00, respectively, for a total amount of $672,256.00. From this amount the auditor subtracted a partnership loss of $42,023.00.

The Division issued to petitioner a Notice of Deficiency, dated March 4, 1991, asserting State and City income tax due in 1986 for the amounts of $2,373.69 and $403.40, respectively, and State and City income tax due in 1987 for the amounts of $50,239.91 and $2,394.15, respectively. Interest and penalty were added to these amounts for the total amount of tax due

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[3]Using March 6, 1987 as petitioner's retirement date from Zale Corporation, the auditor subtracted 18 Saturdays and Sundays and two holidays (January 1, 1987 and February 22, 1987) from the total number of days from January 1, 1987 through March 6, 1987 (65) for the total number of workdays of 45. The auditor excluded from the total workdays 3 Saturdays and 3 Sundays that she included as New York workdays.

[4]The auditor who conducted the audit retired in 1991 and was not made available to testify as to how she calculated the tax. Instead, her supervisor testified as to how the audit was done.

of $87,247.60.

A conciliation conference was held on January 15, 1992 and the conferee sustained the Notice of Deficiency in a Conciliation Order, dated June 19, 1992.

Petitioner filed a petition, dated September 14, 1992, alleging errors by the Division in calculating the allocation of time petitioner worked in New York to the total number of days worked. Specifically, petitioner alleged that the auditor incorrectly counted as New York workdays

weekends, vacation days or days on which he did not work or was not in New York State, and that the auditor incorrectly included as New York days those days on which petitioner spent only a portion of the day working or days on which his only activity in New York was his early departure from, or late arrival to, New York.

The Division filed an answer, dated January 21, 1993, affirmatively stating, inter alia, that the computation of the allocation of days spent in New York State was based on petitioner's diaries and "Platinum Card" charges and that petitioner has the burden of proving that the deficiency is erroneous or improper.

At the hearing held on July 26, 1993, petitioner submitted excerpts from his diary covering the days the auditor counted as New York workdays. He testified that the entries in the diary were made by either his secretary or himself in anticipation of scheduled events. One diary was kept by petitioner's secretary with only her entries and a second diary was kept by petitioner at his Texas office. Petitioner testified that sometimes he would phone in to his secretary with changes to the diary or make certain changes himself in his own diary when he was in Dallas. Petitioner asserted that the purpose of the diary was to plan his schedule in advance, keep informed of scheduled appointments and travels and to keep a record of his business dealings for future use. He noted that the diary represented a road map of his business dealings. With respect to the accuracy of the diary entries, petitioner noted certain changes to scheduled appointments that were not recorded in the diary, but affirmed that in general the

diary was 95% accurate.

When petitioner worked in Texas, he generally would arrive at his office early in the morning and leave between 5:00 or 5:30 P.M. and only on occasion would he work on a Saturday or Sunday. Petitioner noted in his testimony that he might work four or five Saturdays or Sundays over the course of an entire year. In calculating the number of total workdays outside of New York, the auditor excluded a total of 89 Saturdays and Sundays for 1986 and 18 Saturdays and Sundays for 1987. However, the auditor included every Saturday and Sunday petitioner spent in New York as a New York workday.

In his testimony, petitioner conceded that he worked and/or attended a trade show in New York on the following days either a couple of hours or for the entire day:

| 1986 | 1987 |
|---|---|
| 1/10/86 (2-3 hours) | 1/30/87 (2 hours) |
| 1/31/86 (2 hours) | 2/2/87 (½ day) |
| 2/3/86 | 2/3/87 |
| 2/4/86 (½ day) | |
| 2/5/86 (½ day) | |
| 2/25/86 (3 hours) | |
| 4/10/86 (½ day) | |
| 4/16/86 (½ day) | |
| 5/7/86 | |
| 5/8/86 (1 hour) | |
| 5/28/86 | |
| 6/20/86 (1 hour) | |
| 7/28/86 | |
| 7/29/86 | |
| 8/4/86 | |
| 9/10/86 | |
| 9/11/86 (½ day) | |
| 10/23/86 | |
| 10/24/86 | |
| 12/11/86 (2 hours) | |

In referring to his diary, petitioner testified that on November 4, 1986 he left New York at 3:00 P.M. to return to Texas but that he could not remember what he did prior to his flight inasmuch as there were no notations in the diary on that day other than the flight information. He also noted that a 2:00 P.M. appointment was scheduled in his diary on January 14, 1987 and that the appointment was in connection with his Zale employment, but that he could not recall whether the appointment was kept.

Petitioner testified that he did not work on the following Saturdays or Sundays when he was in New York, but spent the time at his leisure with his wife or attended an appointment or evening engagement that was totally unrelated to his work:

| 1986 | 1987 |
|---|---|
| 1/11/86 | 1/10/87 |
| 2/1/86 | 1/31/87 |
| 2/2/86 | 2/1/87 |
| 7/27/86 | |

Petitioner's diary contained an entry on Saturday, January 11, 1986 of "24 Kt. Club Dinner - Waldorf Astoria" followed by a second entry "'Yes' to M. Zale at 6:00 P." In his testimony, petitioner explained that he attended the 24 Carat Club Dinner, which was a charity fund raiser sponsored by the organization of jewelry manufacturers, that he was not a member of the club (nor was the corporation) and that he purchased the ticket for the dinner out of his own funds. Petitioner also explained that the second notation was to remind him that he would meet Mr. Zale at the dinner at 6:00 P.M. Petitioner further testified, after referring to entries on Saturday, January 10, 1987, that he attended the 24 Carat Club Dinner on that date as well.

With respect to Saturday, February 1, 1986, and Saturday, January 31, 1987, petitioner testified that he attended another charitable function, the annual Juvenile Diabetes Foundation dinner, but did not engage in Zale-related activities.

Petitioner testified that on the following New York days he did not engage in any work-related activity in New York because on those days he either departed from New York on an early morning flight back to Texas, or arrived late in New York and either went straight to his hotel or had dinner with a friend:

| 1986 | 1987 |
|---|---|
| 1/12/86 (7:30 A.M. departure) | 1/8/87 (5:00 P.M. arrival) |
| 2/7/86 (9:30 A.M. departure) | 1/11/87 (7:30 A.M. departure) |
| 2/24/86 (late arrival) | 1/13/87 (9:00 P.M. arrival) |
| 4/9/86 (7:00 P.M. arrival) | 1/29/87 (5:00 P.M. arrival) |
| 4/15/86 (late arrival) | |
| 5/6/86 (5:00 P.M. arrival) | |
| 5/27/86 (7:00 P.M. arrival) | |
| 6/19/86 (5:00 P.M. arrival) | |
| 7/31/86 (11:00 P.M. arrival) | |

9/9/86 (7:00 P.M. arrival)
10/22/86 (5:00 P.M. arrival)
10/25/86 (7:30 AM. departure)
11/3/86 (7:00 P.M. arrival)
12/10/86 (5:00 P.M. arrival)

With the exception of February 24, 1986, petitioner's testimony concerning these arrivals and departures is confirmed by flight information recorded in his secretary's handwriting in the diary.

On January 9, 1986, petitioner testified that he arrived in New York at 12:30 P.M. (arrival flight entered in diary) and spent the afternoon visiting with his wife and did not engage in any work-related activity; that on December 12, 1986 petitioner met with his lawyer and a recruiter prior to his departure for Texas;[5] that on January 15, 1987 he spent the day with his wife and flew back to Texas that evening (6:00 P.M. flight departure entered in diary); and that on February 5, 1987 he left New York for Texas on a 12:30 P.M. flight (confirmed by entry in diary) and did not engage in any work-related activity in New York prior to his departure.

Referring to notations made in his diary, petitioner testified that on the following dates he was not in New York at all but was in either Texas, Louisiana or Toronto:

| 1986 | 1987 |
|---|---|
| 4/12/86 (Texas) | 1/16/87 (Texas) |
| 4/13/86 (Texas) | 1/20/87 (Texas) |
| 4/14/86 (Texas) | 1/22/87 (Texas) |
| 4/30/86 (Texas/Louisiana) | 1/27/87 (Texas) |
| 5/1/86 (Texas) | 1/28/87 (Texas) |
| 5/2/86 (Texas) | 2/6/87 (Texas) |
| 7/30/86 (Texas) | 2/7/87 (Texas) |
| 9/12/86 (Texas) | 2/8/87 (Texas/Toronto) |
| 9/13/86 (Texas) | 2/9/87 (Toronto) |
| 11/5/86 (Texas) | |

[5]In his diary for that date, there are entries for a 2:47 P.M. departure flight and backup flight at 5:59 P.M. The diary also contains an entry in petitioner's handwriting indicating a 10:00 A.M. meeting with Bob Goodkind, petitioner's attorney, and a 12:30 P.M. lunch appointment.

12/13/86 (Texas)[6]
12/29/86 (Texas)

In most cases the entries in the diary confirm petitioner's testimony concerning his location on those dates. However, notwithstanding the absence in the diaries of an entry specifying a location, there are no entries in the diary on any of those days that would indicate petitioner's presence in New York.

Petitioner testified that from September 25, 1986 through September 29, 1986 and from November 6, 1986 through November 12, 1986, he cancelled all meetings in New York to be in Texas preparing with others from Zale Corporation a defense to a new takeover offer that the corporation became aware of on September 24, 1986. A notation in petitioner's handwriting was entered in the diary on November 7, 1986 - "Trip cancelled due to take over fight." Petitioner testified that in that week of

November, he and other Zale representatives presented a plan at meetings with an investment bank firm to obtain a loan to counter the takeover offer. He stated that these meetings took place over several days resulting in his cancelling his trip to New York and the New York appointments that were listed in the diary for those days.

Petitioner testified that on July 25, 1986 he took a flight from Dallas to LaGuardia Airport arriving at 10:00 A.M., stayed at LaGuardia to take a 1:00 P.M. flight to Albany and from there drove to upstate New York to visit his daughter who was attending a summer camp in the Adirondacks. He stated that the next day, Saturday, July 26, 1986, he returned to New York City on a flight from Albany arriving at 7:00 P.M. The flights on July 25, 1986 and July 26, 1986 are confirmed by entries in

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[6] December 13, 1986 fell on a Saturday and petitioner testified that he returned to Texas on the prior day, December 12, 1986 (3:00 P.M. and 6:00 P.M. flight listed in diary), and that although he was in Texas on that date, he did not work at all on that date.

petitioner's diary.

Petitioner testified that he returned to Dallas on July 29, 1986 for meetings in Dallas the next day and returned to New York on July 31, 1986 arriving in Albany, New York at 11:00 P.M. Petitioner explained that he spent from August 1, 1986 through August 3, 1986 on vacation at the Saratoga Racetrack and then worked in New York City on August 4, 1986. The entries in petitioner's diary on July 31, 1986 contained flight information indicating arrival in Albany at 11:00 P.M., entries on August 1, 2 and 3 noting a vacation at Saratoga, and flight information on August 3, 1986 indicating a flight from Albany arriving at 8:15 P.M. in LaGuardia.

Petitioner testified that on April 11, 1986 he did not engage in any work-related activities but instead met with his tenant in New York and drove out to petitioner's New Jersey house which he was leasing to the tenant at that time. Petitioner stated that the purpose of the New Jersey trip was to ensure that the house was in good shape and that periodically he would make such checks. Petitioner then noted that he flew back to Dallas that evening. The diary entries for April 11, 1986 indicated a 10:30 A.M. appointment with the tenant and a flight from LaGuardia departing at 6:00 P.M.

Petitioner further testified that on the following dates he did not engage in any work-related activities but instead cancelled appointments and either spent the day with his wife or met with recruiters in his efforts to seek future employment:

| 1986 | 1987 |
|---|---|
| 2/6/86 | 1/9/87 |
| 12/12/86[7] | 1/15/87[8] |

[7] Petitioner testified that he flew back to Texas after meeting with a recruiter. Entries in his diary confirm the flight back to Texas.

[8] Petitioner testified that after spending the day with his wife he flew back to Texas. The entries

2/4/87

On February 8, 1987, petitioner flew to Toronto[9] to attend a budget meeting with the new owners of Zale Corporation. At that meeting, petitioner and the new owners mutually agreed to terminate petitioner's employment. On March 1, 1987, petitioner signed a letter sent by Jerry W. Davis, a senior vice-president of Zale Corporation, setting forth the terms and conditions of the termination of petitioner's employment. According to the agreement, the termination was effective on February 28, 1987.

In that letter, Zale Corporation agreed to pay petitioner in consideration for petitioner's execution of the termination agreement a lump-sum payment of $250,000.00, less normal wage deductions, before March 12, 1987. The letter further provided for petitioner's continued employment until December 31, 1988 under certain terms and conditions. Petitioner's attendance was not required from February 28, 1987 through December 31, 1988. For the period March 1, 1987 through February 28, 1988, petitioner was to receive semi-monthly payments of $1,458.34 and that if petitioner had not obtained other employment by March 1, 1988, Zale Corporation was to pay petitioner $11,875.00 semi-monthly until December 31, 1988 or until he obtained other employment. If petitioner accepted other employment before December 31, 1988, then he was to terminate his employment with Zale Corporation and Zale's obligation to "make the foregoing salary payments" would be diminished by the amount of any remuneration petitioner received "directly or constructively from any other employer for [his] services during such period." Zale Corporation also continued to provide to petitioner during his "continued employment" certain benefits such as medical and life insurance programs and a company car. Petitioner agreed to

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in his diary for that day confirm the flight departure at 6:00 P.M.

[9]Petitioner's diary entries and testimony confirm that he was in Toronto on February 8 and 9, 1987 and was not in New York on those dates.

waive any severance pay in accordance with the following terms as provided in the letter:

"Severance Pay

"In consideration for the payments the Company agrees to make to you hereunder, you hereby agree to:

"(a) Waive any right that you may have to receive severance pay; and

"(b) Waive any right to receive any payment for all currently accrued, vacation and personal holiday benefits, and it is further understood that no vacation or personal holiday benefits will be accrued to you from the date of this letter."

During the period from the end of February 1987 through the end of December 1988, petitioner performed some consulting services for Zale Corporation in Texas but did no travelling for the corporation.

In addition to his salary and other wages, petitioner reported on his 1987 income tax return the sale of Zale stock for the sum of $1,200,000.00. The new owners of Zale Corporation purchased from petitioner 24,000 shares of unvested stock at $50.00 a share. Petitioner had previously received from Zale Corporation two grants of stock: one grant of 15,000 shares in January of 1984, 20% of which was to vest each year for five consecutive years from 1985 through 1989; and a second grant of 15,000 shares in May-June 1986 of which 20%, or 3,000 shares, was to vest each year over the next five consecutive years from 1987 through 1991. These stock grants were given as an incentive to ensure the continued successful employment of petitioner.[10] According to the stock plan, if petitioner terminated his employment prior to the date each 20% of the stock vested, the unvested stock would be forfeited and returned to the corporation. If, however, another corporation, individual, firm or entity acquired more than 50% of the outstanding voting securities of the corporation, the unvested stock would become "immediately freely transferable and non-forfeitable." Thus, in accordance with the

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[10]The Division submitted into the record a document, dated March 10, 1982, entitled "Zale Corporation Restricted Stock Plan". In that document, it was stated that stock grants may be given to key executive employees of the company taking into account the "duties of the respective individuals, their present and potential contributions to the success of the Company or the subsidiary and such other factors as the Committee shall deem relevant in accomplishing the purposes of the Plan."

corporation's stock plan, petitioner was free to sell the 24,000 shares that were unvested just prior to the takeover. With respect to this sale, petitioner testified as follows:

Q. "Now, when the company was taken over by the Toronto-based organization in 1987, did that have any impact on the amount of Zale stock you had that was not yet vested?"[11]

A. "Yes. As the Court probably knows, in takeovers of this kind the arriving company doesn't want to have minority stockholders, so it bought out all of those options, all of those grants."

Q. "Is that the transactions that resulted in you having income in 1987 of a million two?"

A. "Yes, because that would have related to 24,000 shares of unvested stock at $50 a share."

Q. "What price was the stock bought out at?"

A. "$50 a share."

Q. "Was that takeover price?"

A. "That is the takeover price." (Tr., p. 119.)

* * *

Q. "And would it be fair to say that million two that you received in income from the purchase of these stocks by the company that took over Zales had to do with re remuneration for your service to the company in the year 1987?"

A. "No. The purpose -- the purpose of these stock grants was to tie the executive into the performance of the stock share price so that both the stockholder and the executive had a commonality of interest in getting the stock price high. It was an investment that was given to each executive to keep them employed by the company for an extended period of time. So these grants ran out five years from the date you got the grant. You were not able to fully vest for five full years, and that was a way of keeping the executive with an equity investment interest in the company."

Q. "Is that $1,200,000 in gain that you realized, would that be akin to termination pay?"

A. "No, it had nothing to do with termination."

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[11] The transcript contains the term "invested"; however, it is clear from the context that the word should be "vested".

Q. "Salary?"

A. "No."

Q. "Did it have anything to do with your services as an employee?"

A. "No." (Tr., pp. 120-121.)

SUMMARY OF THE PARTIES' POSITIONS

Petitioner argues in brief that the auditor erred in calculating the number of days worked in New York by including days that he was not in New York, days on which he was vacationing, weekend days when he did not work, days on which his only activity in New York was to arrive or depart by plane, and days on which he was not involved in work-related activities. Petitioner notes that the audit began as a domicile case and concludes that the auditor made no attempt to determine if petitioner worked in New York, but instead made her calculations based on petitioner's mere presence in New York. Petitioner further argues that the auditor erroneously allocated income to New York for 1987 based on a 45-day work year when he was employed by Zale Corporation for the entire year. Of the days that petitioner identified as New York workdays, petitioner claims that a nonresident is permitted to allocate income on the basis of hours or fractions of a day. According to this method, petitioner alleges that in 1986 he worked only 12.76 days in New York out of 254 days and in 1987 he worked only 2 days out of 254 workdays resulting in an allocation ratio of 5.02% and 0.78%, respectively.

At the commencement of the July 26, 1993 hearing, petitioner's counsel presented two other issues. He argued that the payment by Zale Corporation for the unvested stock grants given to petitioner should not be allocated to the year 1987 and instead should be allocated over the entire course of petitioner's employment from 1984 through 1987. During petitioner's cross examination concerning the stock grants, petitioner's counsel appeared to raise another issue with respect to the $1,200,000.00 payment -- whether the payment was "subject to a nonresident tax at all" (tr., p. 142). Petitioner's counsel also requested "to preserve" for a post-hearing submission "if appropriate" the constitutionality of "taxing a corporate executive who comes into New York for the purpose of an incidental trade show for his work and/or the

constitutionality of taxing such a person for a full day based upon no work activity taking place." When counsel was asked whether the constitutionality issue would be the subject of an exchange of briefs, he responded "Yes." Neither petitioner's brief nor reply brief raise any issues as to the constitutionality of the Division's actions. Thus, inasmuch as petitioner has not raised the issue in his briefs, it is no longer "preserved" for review.

The Division's counsel questions the credibility of petitioner's testimony and diaries implying that it would be incongruous for a chief executive officer of a nationwide retailing company to indulge himself by spending "personal leisure time" in New York. Counsel further argues that because petitioner's employment ceased as of March 6, 1987, the auditor's use of 45 days as the total number of days worked in and out of New York is correct.

CONCLUSIONS OF LAW

A. Tax Law former § 632(a)(1), applicable to the 1986 and 1987 tax years in question, provided that the New York adjusted gross income of a nonresident individual shall include the net amount of items of income and gain entered into the Federal adjusted gross income "derived from or connected with New York sources." Tax Law former § 632(b)(1)(B) provided that items of income and gain derived from or connected with New York sources shall be those items attributable to "a business, trade, profession or occupation carried on" in New York State. Tax Law former § 632(b)(2) provided that income, including gains from the disposition of intangible personal property, "shall constitute income derived from New York sources only to the extent that such income is from property employed in a business, trade, profession or occupation carried on in this state."

Tax Law former § 632(c) provided that:

> "If a business, trade, profession or occupation is carried on partly within and partly without this state, as determined under regulations of the tax commission, the items of income, gain, loss and deduction derived from or connected with New York sources shall be determined by apportionment and allocation under such regulations."

The regulations provided that if a nonresident employee, including a corporate officer, "performs services for his [or her] employer both within and without New York State, [the]

income derived from New York State sources includes that portion of [the] total compensation for services rendered as an employee which the total number of working days employed within New York State bears to the total number of working days employed both within and without New York State" (20 NYCRR former 131.18[a]). The regulation further provided that, in computing the allocation of income, "no account is taken of nonworking days, including Saturdays, Sundays, holidays, days of absence because of illness or personal injury, vacation, or leave with or without pay."

Here, petitioner concedes in his testimony that he engaged in Zale-related business in New York on the following days, some of which involved a few hours or one-half day's work:

| 1986 | 1987 |
|---|---|
| 1/10/86 (2-3 hours) | 1/30/87 (2 hours) |
| 1/31/86 (2 hours) | 2/2/87 (½ day) |
| 2/3/86 | 2/3/87 |
| 2/4/86 (½ day) | |
| 2/5/86 (½ day) | |
| 2/25/86 (3 hours) | |
| 4/10/86 (½ day) | |
| 4/16/86 (½ day) | |
| 5/7/86 | |
| 5/8/86 (1 hour) | |
| 5/28/86 | |
| 6/20/86 (1 hour) | |
| 7/28/86 | |
| 7/29/86 | |
| 8/4/86 | |
| 9/10/86 | |
| 9/11/86 (½ day) | |
| 10/23/86 | |
| 10/24/86 | |
| 12/11/86 (2 hours) | |

Petitioner argues that Advisory Opinion TSB-A-83-(1)-I (February 4, 1983) permits a nonresident to allocate income on the basis of hours or fractions of a day. Thus, assuming an 8½-hour day, petitioner claims that he worked in New York for 12.76 days in 1986 and 1.97 or 2 days in 1987. Although petitioner's testimony is credible, there is no reason to allocate income using fractions based on an 8½-hour workday. Petitioner was not an hourly employee and it is fair to assume in these circumstances, considering the reason for the New York visits and nature of his work, that a one- to three-hour meeting should constitute a half-day's work.

Thus, petitioner essentially admits to working in New York in 1986 for 14.5 days and in 1987 for 2 days.[12]

Three additional days will be added to the days petitioner conceded as New York workdays: January 11, 1986 (½ day), November 16, 1986 (full day) and January 10, 1987 (½ day) and January 14, 1987. Because petitioner could not recall whether he performed services for Zale Corporation when he was in New York on November 16, 1986, the entire day is considered a New York workday (see, Finding of Fact "16"). Similarly, petitioner could not recall whether he kept a 2:00 P.M. appointment scheduled in his diary on January 14, 1987. Inasmuch as he testified that the appointment related to his Zale employment and no other explanation was given for his activities on that day, the entire day of January 14, 1987 is considered a New York workday.

Although January 11, 1986 and January 10, 1987 fall on Saturdays and petitioner claimed he spent the day at his leisure, he attended two annual benefit dinners sponsored by the 24 Carat Club in the evenings. Petitioner claimed that his attendance at the dinners was not work related and that he purchased the tickets out of his own funds. However, petitioner did attend the January 11, 1986 dinner with Mr. Zale and it is apparent that the dinners were attended by people in the retail jewelry industry. Inasmuch as petitioner noted that the reason for his more frequent trips in 1986 and 1987 was to provide a physical presence in New York to convey a sense of the financial well-being of the company, it is reasonable to assume that his attendance, as well as that of Mr. Zale, at these annual dinners furthered these goals. Thus, his attendance at the dinners each constituted one-half

day's work in New York. Thus, the total number of workdays in New York is increased to 16

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[12]Fractionalizing the New York workdays into one-half days will affect the denominator, or total number of workdays in and out of New York State, to the extent that petitioner did not work the other half of the day or travel between Dallas and New York on those days (see infra, Conclusions of Law "B" and "C").

days in 1986 and 3½ days in 1987.

B. The question is whether petitioner met his burden of proving that he was not engaged in work-related activities during the remaining time periods that the auditor included in her allocation ratios for 1986 and 1987. Based on petitioner's demeanor and forthrightness during his testimony (see, e.g., Finding of Fact "16") and his general clarity and consistency in reconstructing the events from the entries in his diary, I find petitioner's testimony to be both reliable and credible (see, Matter of Moss, Tax Appeals Tribunal, November 25, 1992). Moreover, the fact that there were subsequent entries or unmarked changes to these diaries do not effect the contemporaneous or reliable nature of these diaries that were kept by petitioner and his secretary for business purposes (see, id.).

Given the fact that petitioner was not a punch-card employee of Zale Corporation and taking into account that his trips to New York were for the limited purpose of attending trade shows and providing a personal reassurance to suppliers of the company's financial viability, petitioner's testimony that his New York workday consisted of a one- to three-hour meeting or one-half day's work is credible. In addition, it is clear that petitioner used these business trips as opportunities to attend to his personal affairs, e.g., reconciliation efforts with his wife, exploring alternate employment opportunities, the rental and sale of his New Jersey house, and social engagements based on long-standing contacts from his prior residence in the metropolitan New York City area. Taking into account these circumstances and petitioner's testimony, the following days should be excluded as nonworking days from both the numerator and denominator[13] of the allocation ratio:

| 1986 | 1987 |
|---|---|
| 2/1/86 (Saturday) | 1/9/87 (with wife) |
| 2/2/86 (Sunday) | 1/31/87 (Saturday) |
| 2/6/86 (with wife) | 2/1/87 (Sunday) |
| 7/25/86 (travel to NY to visit daughter at camp) | 2/4/87 (no work) |

[13]Thus, for 1986, the denominator in the allocation ratio is reduced from 258 to 248. For 1987, the denominator is reduced by four days.

7/26/86 (with daughter at camp)
7/27/86 (Sunday)
8/1/86 (vacation in Saratoga)
8/2/86 (vacation in Saratoga)
8/3/86 (vacation in Saratoga)
12/13/86 (Saturday)[14]

An additional reduction in the denominator is required as a result of excluding certain one-half days as non-workdays (see Conclusion of Law "A"). The following one-half days are excluded as non-workdays -- January 10, 1986, January 11, 1986, February 4, 1986, February 5, 1986, April 10, 1986, December 11, 1986, January 10, 1987, January 30, 1987 and February 2, 1987. On these days petitioner testified that he only worked one-half day in New York and spent the remainder of the day at his leisure or on personal business. Thus, the denominator is reduced from 248 to 245 for 1986 and by 5½ days in 1987.

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[14] Petitioner provided credible testimony, confirmed by flight information contained in his diary, that he had returned to Texas from New York the night before on the 6:00 P.M. flight and that he did not work that Saturday in Texas. Thus, this day is considered a non-workday as well as a nonwork New York day.

C. Based on petitioner's testimony and diary entries, the following days should not be counted as New York workdays inasmuch as he performed no work-related duties in New York other than travelling from Dallas to New York or from New York to Dallas (see, Findings of Fact "18", "23" and "24"):

| 1986 | 1987 |
|---|---|
| 1/9/86 | 1/8/87 |
| 1/12/86 | 1/11/87 |
| 2/7/86 | 1/13/87 |
| 2/24/86 | 1/15/87 |
| 4/9/86 | 1/29/87 |
| 4/11/86 | 2/5/87 |
| 4/15/86 | |
| 5/6/86 | |
| 5/27/86 | |
| 6/19/86 | |
| 7/31/86 | |
| 9/9/86 | |
| 10/22/86 | |
| 10/25/86 | |
| 11/3/86 | |
| 12/10/86 | |
| 12/12/86 | |

This conclusion is supported by the example set forth in the Division's regulations in effect during the tax years in question (20 NYCRR former 131.18[a] [example 1]). Although these travel days are not considered New York workdays, they are counted as workdays in the denominator of the allocation ratio.

D. The Division's auditor counted March 4, 1987 as a New York workday. Inasmuch as it is clear from the termination agreement that petitioner no longer performed services for Zale Corporation after February 28, 1987, the day cannot be counted as a New York workday. Similarly, the denominator must also be adjusted downward. The auditor

counted certain Saturdays and Sundays as New York workdays, but incorrectly excluded those days from the total number of workdays in and outside of New York (see, Finding of Fact "8", ftn. "3"). Thus, the following Saturdays and Sundays are included in the denominator of the allocation ratio as days petitioner worked either in New York or outside New York as established by his testimony and diary entries:

1/10/87 (New York workday)
1/11/87 (travel from New York to Dallas)
2/7/87 (Texas workday)
2/8/87 (travel from Dallas to Toronto)

From the total number of days in January and February of 1987 (59), five and one-half days are excluded as non-workdays in New York (see, Conclusion of Law "B"), two holidays are excluded (1/1 and 2/22) and nine Saturdays and Sundays are excluded as non-workdays in or outside of New York. Thus, the total number of workdays in 1987 is 42.5 days.

E. Finally, petitioner demonstrated by his testimony and the entries in his diary that on the following days he was not in New York at all but was in either Texas, Louisiana or Toronto (see, Findings of Fact "19", "20" and "25"):

| 1986 | 1987 |
|---|---|
| 4/12/86 | 1/16/87 |
| 4/13/86 | 1/20/87 |
| 4/14/86 | 1/22/87 |
| 4/30/86 | 1/27/87 |
| 5/1/86 | 1/28/87 |
| 5/2/86 | 2/6/87 |
| 7/30/86 | 2/7/87 |
| 9/12/86 | 2/8/87 |
| 9/13/86 | 2/9/87 |

9/25 - 9/29/86[15]
11/5 - 11/12/86
12/29/86

Thus, these days may not be considered New York workdays. Accordingly, in contrast to the auditor's allocation ratios, the allocation ratio of New York workdays to total work days in 1986 is 16 divided by 247,[16] or 6.478%, and the allocation ratio in 1987 is 3.5 divided by 42.5, or 8.23%. Applying the 1986 allocation ratio to the 1986 income of $321,225.00, the New York wages for 1986 are $20,808.95 instead of the auditor's calculation of $89,644.00. Applying the 1986 partnership loss of $42,595.00 (as did the auditor) to that amount, there is no tax deficiency for 1986. Similarly, applying the 1987 allocation ratio to the 1987 wages of $391,689.00, the 1987 New York taxes are $32,236.00 to which a partnership loss of $42,023.00 should be applied.

F. Petitioner argues that because he worked for Zale Corporation the entire year in 1987, the Division's auditor incorrectly calculated the allocation ratio by using a denominator of 45 days rather than 254 (365 days less

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[15] Petitioner testified that his trip to New York was cancelled for this period and that he remained in Texas to prepare a defense to a takeover offer that the company became aware of on September 24, 1986. Although his diary does not have an entry indicating that the New York trip in September was cancelled, his testimony is both credible and sufficient in the circumstances of this case. He provided sufficient detail throughout his testimony concerning the takeover attempt that ultimately succeeded within a few months of these days. Considering the monumental impact a takeover would have on petitioner, there is no reason to doubt the accuracy of petitioner's memory concerning his whereabouts during the course of events at this time.

[16] Thirteen days are subtracted from the auditor's calculation of 258 total work days in 1986 (see, Conclusion of Law "B"). In calculating the total number of workdays, the auditor subtracted 89 Saturdays and Sundays as non-workdays when, according to the checkmarks on her worksheet only 87 Saturdays and Sundays were not checked off as NY workdays. Thus, it appears that the auditor miscalculated the number of Saturdays and Sundays that were non-workdays according to her chart. Therefore, two more days are added to the total number of workdays in 1986 increasing that number from 245 to 247 (see Conclusion of Law "B").

104 weekend days and 7 holidays).[17] Petitioner's theory is rejected. The termination agreement provided that petitioner's termination was effective on February 28, 1987 and that he would be paid on a semi-monthly basis from February 28, 1987 through December 31, 1988, but that his attendance was not required during this period. Petitioner testified that in lieu of the semi-monthly payments, he elected to receive a lump-sum payment. Although petitioner testified that he provided consulting services to Zale Corporation after February 1987, no details were provided as to the nature of the services or as to how often he performed these services. Thus, there is no basis for using 254 as the total number of days petitioner worked in 1987. The fact that petitioner received a $250,000.00 lump-sum payment militates against the theory that these payments were made for services performed after February 1987. Similarly, inasmuch as his attendance was no longer required after February, the semi-monthly payments from March 1, 1987 through the end of that year are more appropriately characterized as a form of severance pay to which the 1987 allocation ratio is to be applied.

G. At hearing, petitioner's counsel, in addition to the allocation issue, appeared to raise a second issue with respect to petitioner's receipt of $1,200,000.00 for the sale of the 24,000 shares of Zale stock.

Primarily, petitioner's counsel argued at hearing that the allocation ratio the Division applied to the $1,200,000.00 was incorrect because petitioner worked for Zale Corporation the entire year 1987. In the course of petitioner's cross examination, however, petitioner's counsel appeared to raise an issue concerning whether the $1,200,000.00 was subject to a nonresident tax at all. Neither party briefed this issue. Thus, it would appear that this issue has been waived, if raised at all. However, in the interest of completeness, I will address whether the $1,200,000.00 was subject to nonresident income tax as income "derived from or connected with New York sources."

The Tax Appeals Tribunal has

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[17]As noted in Conclusion "D", the denominator used for 1987 has been recalculated to 42.5.

held that:

> "in determining whether income is 'derived from or connected with New York sources' it is necessary to identify the activity upon which the income was secured or earned . . . [and that] in making this determination, the consideration given by petitioner in exchange for the right to the income at issue is the controlling factor" (Matter of Laurino, Tax Appeals Tribunal, May 20, 1993).

Here, petitioner's right to the stock was conditioned on his continued employment over the course of a five-year period; however, the stock became freely transferable by petitioner in the event the corporation was acquired by another corporation, individual, firm or entity. The initial stock grants were given to petitioner as a valued employee for his present and potential contribution to the success of the company (see, Finding of Fact "26", ftn. 10), and were conditioned upon his continued employment. This condition was intended to encourage future contributions by petitioner to the success of the company. However, the event that triggered the 24,000 shares of stock to vest earlier than the successive year terms over the remainder of the five-year period was the acquisition of the company. Thus, petitioner's right to the stock was no longer conditioned on his future services but vested on the acquisition date based upon the initial terms of the stock grants in 1984 and 1985. The stock grants were therefore based upon his services to the company up until the acquisition by new owners. To the extent these services were performed in New York, the income is "derived or connected with New York sources." Rather than use the allocation ratio for 1987 alone, it would be more appropriate to average the allocation ratios of 1986 and 1987, as did the Division's auditor for New York benefits received in 1987, and apply the averaged allocation ratio (7.35%) to the $1,200,000.00.[18]

H. The petition of Kenneth J. Cort is granted to the extent indicated in Conclusions of Law "A" through "E" and "G" and is otherwise denied, and the Notice of Deficiency, dated March 4, 1991, should be adjusted accordingly.

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[18]Assuming, arguendo, that this average should reflect petitioner's services from the date the unvested stock was granted to the date on which the shares became transferable, there is no record evidence to substantiate what the allocation ratios would have been in 1984 and 1985.

DATED: Troy, New York
April 14, 1994

/s/ Marilyn Mann Faulkner
ADMINISTRATIVE LAW JUDGE