STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
RICHARD F. AND DIANE L. HOROWITZ	:	DETERMINATION DTA NO. 813726
for Redetermination of a Deficiency or for Refund of New York State Personal Income Tax under Article 22 of the Tax Law and City of New York Nonresident Earnings Tax under Chapter 46, Title U of the Administrative Code of the City of New York for the Year 1976.	:	

Petitioners, Richard F. and Diane L. Horowitz, 18 Emerson Terrace, Bloomfield, New Jersey 07003-2921, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law and City of New York nonresident earnings tax under Chapter 46, Title U of the Administrative Code of the City of New York for the year 1976.

A hearing was held before Brian L. Friedman, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on January 16, 1996 at 1:15 P.M., with all briefs to be submitted by April 20, 1996, which date began the six-month period for the issuance of this determination. Petitioner Richard F. Horowitz appeared pro se and on behalf of his wife, Diane L. Horowitz. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Michael J. Glannon, Esq., of counsel).

ISSUE

Whether certain income received by petitioner Richard F. Horowitz during the year at issue was properly determined by the Division of Taxation to be New York source income and, accordingly, subject to the imposition of New York State personal income tax and City of New York nonresident earnings tax.

FINDINGS OF FACT

1. On August 29, 1994, the Division of Taxation ("Division") issued a Notice of Additional Tax Due to Richard F. and Diane L. Horowitz[1] which asserted additional New York State personal income tax in the amount of $4,898.00 and additional City of New York nonresident earnings tax of $2,990.00, plus interest imposed on both taxes, for a total amount due of $31,093.66 for the year 1976. Attached to the Notice of Additional Tax Due was an explanation and computation which stated as follows:

> "Since you have not furnished the information requested in our letters of April 15 and June 1, 1994, we have recomputed your New York tax liability to include the Federal Audit Changes made to the Weiss, Rosenthal, Heller, Schwartzman Partnership.

	Federal	New York
Total New York income, previously adjusted	$ 70,477.00	$ 69,930.00
Federal audit adjustment	33,796.00	33,796.00
New York income, adjusted	$104,273.00	$103,726.00
Limitation Percentage: $103,726.00 = 99.48% $104,273.00		
Itemized deductions ($11,842.00 X 99.48%)		11,780.00
Balance		$ 91,946.00
Exemptions ($2,600.00 X 99.48%)		2,586.00
New York taxable income		$ 89,360.00
New York State tax		$ 11,714.00
New York City tax		3,442.00
Total tax		$ 15,156.00
Tax previously adjusted		7,268.00
ADDITIONAL PERSONAL INCOME TAX DUE		$ 7,888.00"

[1]For the year 1976, Richard F. and Diane L. Horowitz filed a New York State Income Tax Nonresident Return and a City of New York Nonresident Earnings Tax Return under the filing status "married filing joint return". Since the income at issue was earned by Richard F. Horowitz and since Diane L. Horowitz is a party to this proceeding only by virtue of the aforementioned filing status, all references to "petitioner" shall refer solely to Richard F. Horowitz.

2. Previously, by letter dated May 19, 1992, the Division had requested that petitioner provide additional information relating to a Federal audit change. This letter, from the Central Income Tax Section of the Audit Division, stated, in part, as follows:

> "Information available indicates the Internal Revenue Service has adjusted your Federal income tax return(s) for the year(s) shown above. This information also indicates that the net income/loss from the partnership, Weiss, Rosenthal, Heller, Schwartzman of which you are a member partner, was adjusted.
>
> "A search of our files fails to show that you reported these changes to New York State. Section 659 of the New York State Tax Law states that Federal audit changes must be reported to New York State within 90 days of the date of the final Federal determination."

3. For the year 1993, petitioner filed an individual New York State tax return; the Division determined that petitioner had made an overpayment of tax in the amount of $22,834.00 for 1993. On November 10, 1994, the Division issued a Statement of Income Tax Adjustment (see, Division's Exhibit "D") which advised petitioner that the overpayment was being applied to the outstanding tax liability for the year 1976. As a result thereof, a Consolidated Statement of Tax Liabilities, dated January 3, 1995, advised that a balance of $8,695.17 (consisting solely of interest on the State income tax portion) was due and owing as of that date (see, Division's Exhibit "D").

4. During the year at issue and for several years prior thereto, petitioners were nonresidents of the State of New York, having resided in Bloomfield, New Jersey since April 1971. For the tax year 1976, petitioner, an attorney at law, was a partner in the law firm of Weiss, Rosenthal, Heller, Schwartzman & Lazar (the "law firm"). The law firm's offices were located at 295 Madison Avenue, New York, New York; it had no offices outside of the City and State of New York.

5. For the tax year ended December 31, 1976, petitioner and 16 other partners in the law firm invested in certain tax shelter partnerships, to wit, Brighton & Fairview, a California movie deal, Spruce & River, a Kentucky coal mine, Spanish Village, an out-of-state partnership and Future Tense, a New York based record deal. The Internal Revenue Service determined that the law firm had ordinary income which it had not reported as distributions to the partners.

As a result of these Federal audit changes, the Division of Taxation issued the Notice of Additional Tax Due (see, Finding of Fact "1") to petitioners.[2]

6. Form 4605-A, Examination Changes - Partnerships, Fiduciaries, Small Business Corporations, and Domestic International Sales Corporations and Form 886-S, Partners' Shares of Income, Deductions, and Credits (see, Division's Exhibit "G"), the Internal Revenue Service documents which formed the basis for the issuance of the Notice of Additional Tax Due by the Division, were issued by the Internal Revenue Service to the law firm rather than to each of the 17 partners who had taken part in the investments.

SUMMARY OF THE PARTIES' POSITIONS

7. Petitioners contend as follows:

a. Because petitioners were nonresidents of New York, the income earned by them from non-New York businesses is not subject to New York State and City of New York taxes since, pursuant to Tax Law § 632(a)(1), in determining New York source income of a nonresident partner, only the portion derived from or connected with New York sources can be included;

b. The income at issue was not derived from investments made by the law firm, but was, instead, from investments by individuals which were made, for purposes of convenience, through the law firm; and

c. In the alternative, even if determined to have been investments of the New York law firm, with the exception of the income from Future Tense, the income was not derived from or connected with New York sources.

The Division of Taxation maintains:

---

[2]The explanation and computation attached to the Notice of Additional Tax Due indicates that, as a result of the Federal audit adjustment, petitioner had additional New York income in the amount of $33,796.00. Petitioner's Exhibit "1", prepared by the law firm's accountants subsequent to the Federal audit changes, sets forth the amounts derived by each of the partners from the partnerships. This accounting document indicates that petitioner received $34,518.00 from the partnerships rather than $33,796.00. However, since the amount of the adjustment was not raised as an issue by either party to this proceeding, it shall be assumed that, in the event that the Division correctly determined that this income was New York source income, the amount at issue is correct.

a. Petitioners have failed to prove that the income was generated from investments made in an individual capacity; and

b. The law firm had no offices outside of New York; accordingly, all income derived from it is considered to be New York source income.

CONCLUSIONS OF LAW

A. Tax Law former § 632(a)(1)(A), in effect during the year at issue, provided that the New York adjusted gross income of a nonresident individual included his "distributive share of partnership income, gain, loss and deduction, determined under section six hundred thirty-seven."

B. Tax Law former § 637(a)(1) provided as follows:

> "In determining New York adjusted gross income of a nonresident partner of any partnership, there shall be included only the portion derived from or connected with New York sources of such partner's distributive share of items of partnership income, gain, loss and deduction entering into his federal adjusted gross income, as such portion shall be determined under regulations of the tax commission consistent with the applicable rules of section six hundred thirty-two."

C. Tax Law former § 632(b)(1) stated that items of gain, loss and deduction "derived from or connected with New York sources" consisted of items attributable to the ownership of an interest in real or tangible personal property in the State or "a business, trade, profession or occupation carried on in this state."

D. 20 NYCRR former 131.4(a) stated as follows:

> "(1) The New York adjusted gross income of a nonresident individual includes items of income, gain, loss and deduction entering into his Federal adjusted gross income which are attributable to a business, trade, profession or occupation carried on in New York State.
>
> "(2) A <u>business, trade, profession or occupation</u> (as distinguished from personal services as an employee) is carried on within New York State by a nonresident when such nonresident occupies, has, maintains or operates desk space, an office, a shop, a store, a warehouse, a factory, an agency or other place where such nonresident's affairs are systematically and regularly carried on, notwithstanding the occasional consummation of isolated transactions without New York State. This definition is not exclusive. Business is carried on within New York State if activities within New York State in connection with the business are conducted in New York State with a fair measure of permanency and continuity. A taxpayer may enter into transactions for profit within New York State and yet not be engaged in a trade or business within New York State. If a taxpayer pursues an undertaking continuously as one relying on the profit therefrom for such taxpayer's

> income or part thereof, such taxpayer is carrying on a business or occupation. However, see section 131.10 of the Part with regard to the effect of the purchase and sale of property by a nonresident of such nonresident's own account."

Since the law firm had no offices outside the State of New York, it is indisputable that this nonresident petitioner carried on his profession within the State.

E. As the Division correctly points out, the income in question in this matter resulted from an Internal Revenue Service adjustment to the law firm's ordinary income for 1976 (and for 1975 as well). The law firm's name is set forth on Form 4605-A (see, Division's Exhibit "J"); the changes refer to Form 1065 which is a U.S. Partnership Return of Income. Despite petitioner's statements that the investments were made in the law firm's name for convenience purposes only and were, in reality, investments made by a group of individuals, there is no documentary evidence to corroborate such statements. Such documentary evidence could include, but not be limited to, personal checks payable to the tax shelter partnerships constituting amounts invested by petitioner or records of the tax shelter partnerships which indicate that petitioner and/or the other law firm partners were limited partners of these tax shelters in an individual capacity. Petitioner's testimony, standing alone, cannot and does not refute the documentary evidence submitted by the Division which indicates that the investments in the tax shelter partnerships were made in the name of the law firm and, accordingly, constituted additional ordinary income to the law firm. Petitioner has, therefore, failed to sustain his burden of proof, imposed pursuant to Tax Law § 689(e), to show that the income at issue was anything other than a distributive share of partnership income from the law firm in which he was a partner in 1976. Since Tax Law former § 632(a)(1)(A), in effect for the year at issue, provided that the New York adjusted gross income of a nonresident individual included his distributive share of partnership income, it must be found that petitioner's share of the income derived by the law firm from its investments in the four tax shelter partnerships was properly included by the Division in petitioner's New York adjusted gross income for 1976.

F. Petitioner also argues that, even if it is determined (and it has so been determined; see, Conclusion of Law "E") that the investments which yielded the income in question were those

of the law firm rather than of petitioner, in an individual capacity, such income is, nevertheless, not subject to tax because (with the exception of the income derived from Future Tense) it was not New York source income. Once again, petitioner's argument is without merit.

As previously pointed out (see, Conclusion of Law "C"), Tax Law former § 632(b)(1) defines the term "gain, loss and deduction derived from or connected with New York sources" to include "a business, trade, profession or occupation carried on in this state". Having been a partner in a law firm with offices exclusively in New York, petitioner, without question, was carrying on a profession in New York (see, 20 NYCRR former 131.4(a); Matter of Hickey, Tax Appeals Tribunal, April 23, 1992; Weil v. Chu, 120 AD2d 781, 501 NYS2d 515). While it is true that investment in tax shelter partnerships was, in all probability, not the primary business of the law firm, it has heretofore been found that the law firm did make such investments and did derive income therefrom. All of the income of the law firm was New York source income since it had no offices outside of New York. Accordingly, despite the fact that three of the four tax shelter partnerships were located in other states, the income from the investments in these partnerships by the law firm is New York source income and petitioner's share of this partnership income was properly subjected to State and City tax by the Division.

G. The petition of Richard F. Horowitz and Diane L. Horowitz is denied and the Notice of Additional Tax Due issued by the Division of Taxation on August 29, 1994, as modified by the Consolidated Statement of Tax Liabilities dated January 3, 1995 (see, Finding of Fact "3") is sustained.

DATED: Troy, New York
October 10, 1996

/s/ Brian L. Friedman
ADMINISTRATIVE LAW JUDGE