STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
NORMAN AND ENID SCHIBUK	:	DETERMINATION DTA NO. 815095
for Redetermination of a Deficiency or for Refund of New York State Personal Income Tax under Article 22 of the Tax Law for the Year 1988	:	

Petitioners, Norman and Enid Schibuk, Route 100B, Moretown, Vermont 05660, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the year 1988.

On March 30, 1997 and April 7, 1997, respectively, the parties waived a hearing and agreed to submit the matter for determination based on documents and briefs to be submitted by November 10, 1997, which date commenced the six-month period for the issuance of this determination. Petitioners appeared by Ranan J. Wichler, Esq., and the Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Michael J. Glannon, Esq., of counsel). After review of the evidence and arguments presented, Winifred M. Maloney, Administrative Law Judge, renders the following determination.

ISSUES

I. Whether petitioners were domiciliaries of New York State for the year 1988, or maintained a permanent place of abode within New York State and spent more than 183 days in New York State, and thus were taxable as residents of New York State.

II. Whether the Division of Taxation properly determined that certain payments which petitioner Norman Schibuk received in 1989 and 1990 were installment payments which must be accrued to the year 1988 pursuant to Tax Law former § 638(c).

III. If petitioners are determined to be nonresidents of New York during 1988, whether certain income items should have been properly allocated to New York as New York source income.

IV. Whether penalties imposed under Tax Law § 685(a) and (b) should be canceled.

FINDINGS OF FACT

1. Petitioner Norman Schibuk is a computer software consultant. Prior to 1981, he was a principal of Compensation Resources, Inc. ("CRI"), a New York software development company. CRI had expertise with MCG software, software applications systems used by the insurance industry. The Management Compensation Group, Incorporated ("MCG"), a Delaware corporation, was the proprietor of the MCG software.

In January 1981, MCG and CRI agreed that CRI would convert, enhance, improve and maintain the MCG software as if CRI's staff constituted the in-house staff of MCG. The agreement set forth mutual covenants and conditions, including the use of Norman Schibuk's services. The agreement also specified that computer equipment which both parties agreed to lease and purchase would be located in CRI's New York office. The agreement was executed by Norman Schibuk as CRI's president. In or about 1984, the parties evolved into partnerships, MCG into Management Partnership ("MP"), an Oregon partnership, and CRI into Compensation Resources Partners ("CRP"), a New York partnership.[1] CRP was one of MP's general partners,

[1]Some documents in the record refer to this partnership as Compensation Resources Partners, while others refer to it as Compensation Resources Partnership.

having a 10% ownership interest.

2. The record does not contain either a partnership or employment agreement between MP and CRP. Nor does it contain any employment agreements between Norman Schibuk and either MP or any of MP's other general partners. In addition, any employment or consulting agreement which Mr. Schibuk may have had with CRP is not part of the record.

3. On August 1, 1986, MP agreed to purchase CRP's partnership interest in MP. A copy of the handwritten memorandum agreement is part of the record.[2] Pursuant to paragraph 1 of the agreement, MP agreed to purchase the 10% interest of MP owned by CRP for $4,000,000.00, of which $1,000,000.00 was to be paid for CRP's capital account with the remaining $3,000,000.00 to be paid as a guaranteed payment. Except for the stipulation that $100,000.00 was to be paid within 30 days of the execution of final documents, the payment terms, i.e., timing and interest rates, were not specifically set out in paragraph 1; rather, reference was made to the payment terms specified in a separate partnership agreement. It appears from paragraph 11 of the agreement, that CRP was also transferring its interest in CRI to MP. Norman Schibuk, as CRP's general partner, executed this agreement.

4. MP made an Internal Revenue Code § 754 election on its 1986 U.S. Partnership Return of Income ("Form 1065"). On the Form 1065, Schedule L, Balance Sheets, at Line 12, "other assets" for the end of the tax year included a deferred expense of $3,000,000.00. According to the 1986 Schedule K-1, Partner's Share of Income, Credits, Deductions, etc., issued by MP to CRP, CRP's distributive share of ordinary income was $715,682.00 and distributions in excess

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[2]This copy is of rather poor quality; the handwriting at times is illegible and at least one page, page 4, containing paragraphs 6, 7, and 8, is missing. In addition, financial statements and balance sheets referenced in various paragraphs of the agreement are missing.

of basis were $1,018,277.00.

On its 1986 Form 1065, CRP treated all distributions it received from MP for 1986 as payments in liquidation of a partnership interest. On the Schedule K-1 issued to Norman Schibuk, CRP listed net long-term capital gain of $1,276,393.50.[3] Petitioners reported that amount on their 1986 Form 1040.

5. The 1988 Schedule K-1 issued by MP to CRP lists under the income section on line 5 guaranteed payments of $966,000.00. There are no other entries on this Schedule K-1. The address listed for CRP is "c/o Norman Schibuk, 8 Cole Drive, Armonk, New York 10504."

The 1988 Form 1065 for CRP lists, as its only source of income, ordinary income from other partnerships in the amount of $966,000.00. On this return, CRP's address is listed as "c/o Labyrinth Systems Inc., 30 Buxton Farm Road, Stamford, CT. O6905." CRP's tax matters partner was listed as Norman Schibuk, whose address was listed as in care of Labyrinth Systems.

6. CRP's 1989 Form 1065 lists, as its only source of income, ordinary income from other partnerships in the amount of $910,000.00. On this return, CRP's address is listed as "c/o Labyrinth, RR1 Box 435, Waitsfield, Vermont 05673."

CRP's 1990 Form 1065 lists as its sources of income ordinary income from other partnerships in the amount of $834,000.00 and an "other loss" of $350,000.00.

7. Prior to and including the years 1986 and 1987, petitioners filed New York State resident income tax returns listing their address as 8 Cole Drive, Armonk, New York.

8. On May 16, 1985, petitioners purchased a second home in Moretown, Vermont. The address of the property was Route 100B, Moretown Village, Moretown, Vermont. Petitioners

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[3]At the end of 1986, Mr. Schibuk had a 75% ownership interest in CRP.

obtained a mortgage from the Vermont Federal Bank in the amount of $68,800.00 for the purchase of the property. Pursuant to the terms of the mortgage, petitioners warranted that they would not occupy the residence as their legal residence. The mortgage was paid in full and discharged on May 13, 1987. The record is silent as to the style and size of this home.

9. On August 28, 1987, petitioners placed the 8 Cole Drive home on the market with a real estate agent, offering it for sale at a price of $1,400,000.00. According to the real estate agent's residential fact sheet, the Cole Drive property was a contemporary style frame home, built in 1983, with a total of 13 rooms, including 5 bedrooms and 4.5 baths.

10. A contract of sale for the Cole Drive property was entered into on October 28, 1988, which resulted in a closing on December 23, 1988. The sale price was $1,075,000.00. Petitioners were not present at the closing; rather Jeffrey J. Kane, Esq., under valid powers of attorney, was present on their behalf.

11. Petitioners have three children, Liza, James and Daniel. During the period in issue, all three were school age. In early September of 1988, a Waitsfield, Vermont physician conducted the children's school physical examinations. In the fall of 1988, they began attending public school in Moretown, Vermont.

12. Petitioners submitted copies of various documents reflecting either a Moretown Vermont post office box number or a Moretown street address of Route 100B. These documents consisted of, among others things, canceled checks drawn on petitioners' joint Citibank checking account, a notice of loan interest rate change from 1st National Bank of Vermont and amendment pages from some of petitioners' insurance policies reflecting an address change. The documents submitted bear dates commencing around June 30, 1988. The documentary evidence submitted by petitioners does not include any sworn documents.

13. On August 12, 1988, Norman Schibuk registered to vote in Vermont. His application for addition to the Moretown, Vermont "checklist" stated that his "principal dwelling place is at Route 100B Moretown VT 05660." A notary public administered the Freeman's Oath to him on the same date. Mr. Schibuk's name was added to the Moretown checklist on August 30, 1988.

14. Petitioners filed Federal personal income tax returns (Form 1040) for the years 1988 through 1990. However, they did not file any New York State tax returns for those years.

15. Petitioners' 1988 joint Form 1040 lists their address as "P.O. Box 484, Moretown, VT 05660." Petitioners claimed a total of five exemptions, three of which were for dependent children. Petitioners reported adjusted gross income of $646,022.00 consisting of: interest income of $4,331.00; dividend income of $1,154.00; taxable refunds of [New York] state and local income taxes of $7,877.00; Schedule C business income of $304,924.00; capital gain of $39,056.00 and, on line 18, partnership income of $288,680.00. The Schedule C Profit or Loss From Business or Profession (Sole Proprietorship) ("Schedule C"), attached to this return, listed the proprietor as Norman Schibuk, principal business activity and profession as computer consultant and the business name and address as Norman Schibuk, PO Box 484, Moretown, VT 05660. The Schedule E Supplemental Income Schedule (from rents, royalties, partnerships, estates, trusts, REMICS, etc.), attached to this return, reported partnership income of $337,928.00 from CRP and an allowable loss of $49,248.00 from the Poinciana-Regency Ltd Partnership. The Schedule D Capital Gains and Losses attached to the return reported long-term gain from sale or exchange of petitioners' Cole Drive home in the amount of $53,550.00, as well as a long-term capital loss carryover of $14,494.00. Form 2119 reported the sale of petitioners' former main home at Cole Drive on December 23, 1988, and listed a basis of $490,000.00, and a selling price of $1,075,000.00. On this form, petitioners also reported that they had bought or

built a new main home and moved into it on December 23, 1988. The cost of the new home was listed as $963,200.00.

16. Petitioners' 1989 Form 1040 lists their address as "P.O. Box 484, Moretown, VT 05660." On the Schedule E attached, partnership income from CRP is listed in the amount of $532,022.00, along with an allowable loss of $1,517.00 from the Florida Baseball Association.

17. Petitioners' 1990 Form 1040 lists the same Moretown, Vermont post office box address as was contained on both the 1988 and 1989 Forms 1040. According to the Schedule E attached to the Form 1040, petitioners had partnership income from CRP in the amount of $132,593.00; an allowable partnership loss of $46.00 from the Florida Baseball Association and income of $12,780.00 from Labyrinth Systems, Inc., an S Corporation. The total partnership and S corporation income listed on line 18 of Form 1040 was $145,327.00.

18. Petitioners filed a Vermont Income Tax Return Resident - Nonresident- Part Year Resident (Form VT-3) for the year 1988 reporting an adjusted Vermont income tax due of $33,531.00. Petitioners determined this amount by multiplying the Form 1040 line 40 amount of $145,786.00 by 23%.

19. Petitioners employed Castro, Langtry & Co. of Rye Brook, New York to prepare their Federal personal income tax returns for tax years 1988, 1989 and 1990. This firm also prepared the Vermont income tax return, as well as CRP's Federal and state partnership returns..

20. On or about December 9, 1991, the Division commenced a field audit of petitioners' 1988, 1989 and 1990 returns. On December 12, 1991, a letter of audit was sent to petitioners at the Armonk, New York address. Subsequently this letter was returned to the Division because a forwarding address was not found. Based on information received from the Armonk postmaster, the auditor sent a final notice letter, dated March 2, 1992, to petitioners, c/o Labyrinth System, 30

Buxton Farm Road, Stamford, CT 06095. The auditor did not receive a response to this letter. After reviewing petitioners' Federal returns for the years 1988 through 1990, the auditor sent another final notice, dated October 14, 1992, addressed to petitioners at P.O. Box 484, Moretown, Vermont. This final notice letter stated that the Division's records failed to show that petitioners filed New York State income tax returns for the period 1988 to 1990 and requested copies of those returns.

21. The audit report includes the contact sheets entitled "Tax Field Audit Record" and "Contacts and Comments of All Audit Actions" which reflected all of the auditor's contacts and comments concerning this audit. According to the contact sheet, on October 16, 1992, the auditor received a telephone call from Enid Schibuk. During the conversation, he requested various items related to the case. She promised to send them as soon as possible.

22. According to the auditor's notes and comments, he received a letter from Mrs. Schibuk, dated October 20, 1992, in which she stated that they "have not resided in NYS since June, 1988." She also stated that the place they "moved" into was a temporary place while construction for the permanent home was in progress. An entry dated April 28, 1993 states that the auditor called Mrs. Schibuk and "she confirmed that when they 'moved 6/88' they occupied a temporary home in Vermont. In 1990 they completed their present home." The auditor further noted that petitioners "claim that the present home which they call their primary home is a direct replacement of the N.Y. home" and therefore there was no capital gain on the sale.

23. The auditor's contact sheets indicate that he received information from and had conversations with petitioners' former representative, Thomas Langtry, regarding petitioners' 1988 New York State tax liability.

24. On November 16, 1993, Mr. Langtry sent a letter to the Division in which he stated

that Mr. Schibuk strongly disagreed with the position taken by the Division with respect to his 1988 New York State tax liability. In this letter, Mr. Langtry stated that both he and Mr. Schibuk had been under the impression that the audit issue was "restricted to the timing of the receipt of income for 1988, i.e. before or after he permanently moved from New York." He further stated that both he and Mr. Schibuk felt that they had already shown that most of the 1988 income was received after the change of residence, and that the enclosed Form IT-203 for 1988 indicated "the resulting tax liability." With regard to the major issue of whether or not the 1988 income should be construed as New York source income, Mr. Langtry set forth the following facts, among others, in support of petitioners' position that none of Mr. Schibuk's business income or partnership-derived income stemmed from New York sources.

> At some point during 1986, CRP discontinued it's [sic] business activities. At that time, all business assets were liquidated. One of the assets owned by CRP, had been an ownership interest in another partnership, "MANAGEMENT PARTNERSHIP" OF PORTLAND, OREGON (hereinafter referred to as "MP"). In essence, there was a buyout agreement, wherein CRP agreed to sell it's [sic] partnership interest back to MP for a specified sum, to be paid over a 5 year period. For the following five years, MP made a lump sum payment to CRP at the end of each calendar year. Consequently, CRP each year received a Federal K-1 . . ., reporting the annual distributions as "guaranteed payments." In essence, they were deferred payments for the 1986 sale of a business interest in the State of Oregon.
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> CRP conducted no business in the State of New York during the five year payout from MP and only reported the annual distribution on a New York partnership return as a matter of continuity. In addition to no business being conducted in New York, the source of the income is the State of Oregon, not New York. Additionally, MR. SCHIBUK reported all of his MP-derived income to the State of Vermont, where he resided at the time of receipt of the income.

Mr. Langtry also requested a conference on behalf of petitioners and requested information about petitioners' appeal rights.

25. Attached to Mr. Langtry's November 16, 1993 letter was petitioners' 1988 Form IT-203 Nonresident and Part-Year Resident income tax return ("Form IT-203"). This return was received by the Division on November 24, 1993. Part C of Form IT-203 asks part-year residents to check the box which describes their situation on the last day of the tax year. Petitioners checked "(2) moved out of New York State and received income from New York State sources during your nonresident period." On the return, they listed the following items as New York source income: taxable interest income of $2,889.00; dividend income of $770.00; taxable refunds of state and local income taxes of $7,877.00; business income of $0.00; capital gain of $39,056.00; and a Schedule E partnership loss of $32,848.00. Petitioners subtracted the taxable refund of state and local income taxes of $7,877.00 and arrived at a New York adjusted gross income of $9,867.00. Petitioners claimed itemized deductions of $8,500.00 and New York dependent exemptions of $3,000.00. They determined their New York State taxable income to be a loss of $1,633.00, with zero tax due.

26. By letter dated February 8, 1994, the Division notified Mr. Langtry that under 20 NYCRR former 148.10(b)(1), when a resident individual changes his status from resident to nonresident and has an installment sale while a resident; he must accrue on the New York State personal income tax return for the resident period the entire amount of the gain remaining unpaid from such installment obligations, regardless of the method of accounting he normally uses in reporting his transactions. Copies of the pertinent regulations were enclosed.

27. On February 16, 1994, the Division issued a Statement of Personal Income Tax Audit Changes, for the year 1988, which contained the following explanation under "Remarks":

> New york [sic] Tax Law provides that when a taxpayer changes from a resident to a nonresident of New York State, he/she must include on the final resident return any item of income, loss or deduction received or accrued up to the time the

> change occured [sic]. This includes the balance of income or gain to be received in the future years from an installment sale.
>
> Our audit revealed that you changed your domicile and residence on December 23, 1988 and spent over 30 days in New York State. Therefore you are being treated as a resident for the entire year.

The statement listed a corrected New York State tax liability, as computed in the attachment, of $105,010.50; penalties for failure to file of $26,252.63 and negligence penalties of $29,813.55, plus interest computed to February 6, 1994 of $49,126.05. The Schedule of Audit Adjustments to New York State Taxable Income contained the following computation:

N.Y. State Adjusted Gross Income per Return		
Audit Increases to N.Y. State Income		
Unreported Income plus Accruals From a 1986 Installment Sale.	$1,323,371.00[4]	
Audit Decreases to N.Y. State Income		
Net Adjustments to N.Y. State Income		1,323,371.00
Corrected Adjusted Gross Income		$1,323,371.00
Itemized Deductions per Return		126,267.00
Audit Increases to Itemized Deductions		
Audit Decreases to Itemized Deductions		
Net Adjustments to Itemized Deductions		0.00
N.Y. Itemized Deduction Adjustment		25,253.40
Corrected Itemized Deductions After Modification		101,013.60
Number of Exemptions Allowed: 3 * Value of Each Exemption: 1000		3,000.00
Corrected N.Y. State Taxable Income		$1,219,357.40

[4]According to the Division's representative, the $1,323,371.00 figure consists of the 1988 Federal adjusted gross income of $646,022.00, plus the deferred payments of $532,022.00 received in 1989 and $145,327.00 received in 1990 from the sale of the MP partnership interest in 1986. It is noted that the Federal adjusted gross income figure of $646,022.00 included a taxable refund of New York State income tax in the amount of $7,877.00. However, the auditor did not make any adjustment to reflect that.

Corrected Taxable Income or Base	$1,219,357.40
Recomputed Tax Liability	101,249.68
Credits Against Tax	
N.Y.S. Resident Credit (IT-112R)	15,827.00
Total Credits Against Tax	15,827.00
Other Taxes or Disallowed Credits	
Tax on Unearned Income	19,587.82[5]
Total Additional Taxes or Disallowed Credits	19,587.82
Corrected tax liability	$105,010.50

28. The Division issued a Notice of Deficiency (Notice No. L-008602436-9), dated March 31, 1994, for personal income taxes due pursuant to Article 22 of the Tax Law for the year 1988 in the amount of $105,010.50, plus interest of $50,474.69 and penalties of $56,740.50. The computation section of the notice contained the following explanation "Field audit of your records disclosed additional tax due."

29. Petitioners timely requested a conciliation conference which was held on August 22, 1995. After the conciliation conference, the conferee issued a Conciliation Order (CMS No. 139742) dated March 15, 1996, sustaining the statutory notice.

30. On September 24, 1997, petitioners submitted various documents consisting of their children's medical and school records; voter registration application for Norman Schibuk; various insurance endorsements and policies; Citicorp bank statements and various Citicorp checks; a Chase Visa bill; Moretown, Vermont tax receipt; a bank deposit slip and a home security contract. These documents have been accepted into the record in this matter.

The Division submitted a brief on October 15, 1997. On November 10, 1997. Petitioners submitted a reply letter with an attachment. The attachment consisted of a letter, dated

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[5]This additional tax was computed on unearned income of $979,391.00 ($1,323,371.00 less earned income of $304,924.00 and capital gain net income of $39,056.00).

November 1, 1997, written by petitioner Enid Schibuk to her representative. The attachment to the reply letter is rejected and was not taken into account in the determination of this matter (***see***, Conclusion of Law "A").

SUMMARY OF THE PARTIES' POSITIONS

31. In their brief, petitioners admit that in the years prior to 1988, their primary residence was 8 Cole Drive, Armonk, New York. They contend that, in February 1988, they decided to move to Moretown, Vermont. However, they waited until June of 1988, the end of their children's school year, to actually move to Vermont. They argue that the Route 100B, Moretown property became their primary residence and their permanent place of abode at that time. They maintain that beginning in September 1988 their children were registered in and began attending public school in Moretown, Vermont as permanent residents. Further, they assert that the Cole Drive property was listed for sale with a real estate broker in August 1987 and was marketed until its sale on December 23, 1988. They assert that they did not utilize the Cole Drive property from June of 1988 until its sale on December 23, 1988. However, they did continue to maintain the utilities on the Cole Drive property in order for the house to be "shown." Petitioners further argue that their tax preparer made an error when he incorrectly stated on the Form 2119 that petitioners moved into their "new main home" on December 23, 1988. They argue that the documentary evidence submitted establishes that petitioners changed their domicile to Moretown, Vermont.

Petitioners assert that the auditor's adjustment of $1,323,371.00 to reflect the accrual of income associated with a 1986 "installment sale" was improper. They contend that they did not have an installment sale. Rather, they were partners in a partnership that transacted an installment sale. Petitioners assert that they were one of several partners in CRP. Petitioners

maintain that CRP's relationship with MP dates back to at least 1981 when, as independent parties, MP's predecessor contracted with CRP's predecessor for services. Petitioners admit that in 1986 CRP liquidated its entire interest in MP. They assert that they reported their allocable share of the sale, $1,276,394.00, on their 1986 income tax returns. Petitioners argue that CRP continued to operate its business after this transaction and that one of its clients continued to be MP. Petitioners assert that they reported their share of income earned from CRP's activities on their 1986, 1987, 1988, 1989 and 1990 Federal tax returns. Petitioners maintain that through November 1987 CRP had offices located in New York. However, in November 1987 CRP moved to 30 Buxton Farm Road, Stamford, Connecticut and continued to operate out of that location until 1990 when it terminated its existence. Petitioners argue that, after November 1987, all of CRP's work was performed in Connecticut, Oregon and Vermont, not in New York State. Therefore, petitioners assert that no portion of their share of CRP's income earned after June 1988 should be subject to tax by New York State because they were nonresidents and the partnership had no activity in New York.

Petitioners contend that they have demonstrated that they changed their domicile and their permanent residence from New York to Vermont in June 1988. Moreover, they assert that the documentation proves that they properly reported their taxable income and that there is no accrual of a gain from an installment sale required because they reported the full gain in 1986. However, if it is determined that some or all of the tax liability is proper, petitioners request that penalties and, to the extent permitted, interest be abated. They assert that their tax returns attempt to reflect the entire income earned by them and that the tax preparer did not intend to misstate income. In fact, they believe that they may have overstated income on their 1989 Federal income tax return.

32. In its brief, the Division contends that petitioners were either domiciled in New York pursuant to Tax Law § 605(b)(1)(A) or were statutory residents of New York pursuant to Tax Law § 605(b)(1)(B). It argues that petitioners' evidence does not support their claim that they changed their domicile to Vermont in June of 1988. It asserts that petitioners were domiciliaries of New York until December 23, 1988, the date of sale of the Cole Drive property. The Division also asserts that since petitioners maintained the Cole Drive property as a permanent place of abode and they failed to prove that they spent fewer than 184 days in New York in 1988, petitioners were statutory residents for that year.

The Division maintains that the date of change of residency is not critical in determining petitioners' New York income tax liability for 1988. The Division argues that pursuant to Tax Law § 638(c) and 20 NYCRR former 148.10, the deferred payments of $532,022.00 received in 1989 and $145,327.00 received in 1990 from the sale of the MP partnership interest in 1986 were to be treated as additional New York income in 1988, the last year of petitioners' New York residency. It contends that the evidence does not support petitioners' contention that there was no installment sale, that the handwritten memorandum agreement of sale between MP and CRP indicated that CRP was selling the MP partnership interest back to MP, and that the purchase price for the partnership interest would be treated as guaranteed payments to be deferred over time. The Division maintains that the guaranteed payments were New York source income. The Division argues that even if petitioners are not required to accrue the 1989 and 1990 deferred payments to New York for the 1988 year, then petitioners would still be required to report those guaranteed payments to New York in 1989 and 1990 because they came from the sale of a New York business interest while petitioners were residents of New York.

The Division contends that the issue of the allocation of New York source income would

arise if it is found that petitioners are nonresidents. It asserts that since petitioners have not provided any reasonable allocation, then all of the income received and reported by petitioners on the 1988 Schedules C and E should be considered New York source income.

The Division argues that petitioners have not shown reasonable cause for their failure to file a 1988 New York income tax return until November 24, 1993, or shown that their failure to do so was not negligent. The Division also argues that petitioners failed to provide any authority for cancellation of interest.

33. In their reply brief, petitioners maintain that the Division erroneously characterized CRP's sale based on misinformation it received from their prior accountant and that the facts are as they have stated them. Moreover, if they did earn additional funds for services rendered, the issue is whether the services have nexus to New York State. They contend that the signing of a contract while they were residents of New York State does not give rise to nexus for all activities thereafter related to the contract. Petitioners assert that "if that was the case, all interstate commerce flowing through New York State would be subject in full to New York taxation" (Petitioners' reply letter, p. 1).

Petitioners request that the penalties be abated because they "believe that the facts and circumstances set forth reflect a situation" where they "have an appropriate position which should be mitigated" (Petitioners' reply letter, p. 2).

CONCLUSIONS OF LAW

A. The parties waived a hearing and agreed to submit documents and briefs in this matter. Each of the parties, when they submitted their documentary evidence, requested permission to submit additional documents. The Division did not submit any additional documents. Petitioners submitted additional documents on September 24, 1997 and also with their reply

letter on November 10, 1997.

The documents submitted by petitioners on September 24, 1997 have been included in the record. The Division had the opportunity to review these records and take them into consideration in the preparation of its brief which was submitted on October 15, 1997. However, the attachment to petitioners' reply letter is rejected. Once the Division submitted its brief, it no longer had the opportunity to confront and respond to any further evidence. A reply brief is meant to respond to the arguments raised by the Division in its brief, not to be the vehicle by which additional evidence is submitted into the record. Petitioners had ample opportunity to submit documentary evidence prior to the due date for submission of their reply brief. There must be some finality in this matter (***see***, ***Matter of Schoonover***, Tax Appeals Tribunal, August 15, 1991). Therefore, the letter attachment submitted with petitioners' reply letter was not considered in making this determination.

B. Tax Law § 605(b) provides, in pertinent part, as follows:

> (1) Resident individual. A resident individual means an individual:
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> (A) who is domiciled in this state, unless (i) he maintains no permanent place of abode in this state, maintains a permanent place of abode elsewhere, and spends in the aggregate not more than thirty days of the taxable year in this state . . . . , or
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> (B) who is not domiciled in this state but maintains a permanent place of abode in this state and spends in the aggregate more than one hundred eighty-three days of the taxable year in this state . . . .
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> (5) Part-year resident individual. A part-year resident individual is an individual who is not a resident or nonresident for the entire taxable year.

C. The Tax Law does not contain a definition of "domicile", but the Division's regulations (20 NYCRR former 102.2[d]) provided, in pertinent part, as follows:

> (d) Domicile. (1) Domicile, in general, is the place which an individual intends to be his permanent home - - the place to which he intends to return whenever he may be absent. (2) A domicile once established continues until the person in question moves to a new location with the bona fide intention of making his fixed and permanent home there. No change of domicile results from a removal to a new location if the intention is to remain there only for a limited time; this rule applies even though the individual may have sold or disposed of his former home. The burden is upon any person asserting a change of domicile to show that the necessary intention existed. In determining an individual's intention in this regard, his declarations will be given due weight, but they will not be conclusive if they are contradicted by his conduct. The fact that a person registers and votes in one place is important but not necessarily conclusive, especially if the facts indicate that he did this merely to escape taxation in some other place.
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> (4) A person can have only one domicile. If he has two or more homes, his domicile is the one which he regards and uses as his permanent home. In determining his intentions in this matter, the length of time customarily spent at each location is important but not necessarily conclusive. As pointed out in subdivision (a) of this section, a person who maintains a permanent place of abode in New York State and spends more than 183 days of the taxable year in New York State is taxable as a resident even though he may be domiciled elsewhere.

Permanent place of abode is defined in the regulations at 20 NYCRR former 102.2(e)(1) as "a dwelling place permanently maintained by the taxpayer, whether or not owned by him, and will generally include a dwelling place owned or leased by his or her spouse."

D. To effect a change in domicile, there must be an actual change in residence, coupled with an intent to abandon the former domicile and to acquire another (***Aetna National Bank v. Kramer***, 142 App Div 444, 445, 126 NYS 970). Both the requisite intent as well as the actual residence at the new location must be present (***Matter of Minsky v. Tully***, 78 AD2d 955, 433 NYS2d 276). The concept of intent was addressed by the Court of Appeals in ***Matter of Newcomb*** (192 NY 238, 250-251);

> Residence means living in a particular locality, but domicile means living in that locality with intent to make it a fixed and permanent home. Residence simply requires bodily presence as an inhabitant in a given place, while domicile requires

bodily presence in that place and also an intention to make it one's domicile.

> The existing domicile, whether of origin or selection, continues until a new one is acquired, and the burden of proof rests upon the party who alleges a change. The question is one of fact rather than law, and it frequently depends upon a variety of circumstances, which differ as widely as the peculiarities of individuals . . . . In order to acquire a new domicile there must be a union of residence and intention. Residence without intention, or intention without residence is of no avail. Mere change of residence although continued for a long time does not effect a change of domicile, while a change of residence even for a short time, with the intention in good faith to change the domicile, has that effect . . . . Residence is necessary, for there can be no domicile without it, and important as evidence, for it bears strongly upon intention, but not controlling, for unless combined with intention it cannot effect a change of domicile . . . . There must be a present, definite and honest purpose to give up the old and take up the new place as the domicile of the person whose status is under consideration . . . . [E]very human being may select and make his own domicile, but the selection must be followed by proper action. Motives are immaterial, except as they indicate intention. A change of domicile may be made through caprice, whim or fancy, for business, health or pleasure, to secure a change of climate, or a change of laws, or for any reason whatever, provided there is an absolute and fixed intention to abandon one and acquire another and the acts of the person affected confirm the intention . . . . No pretense or deception can be practiced, for the intention must be honest, the action genuine and the evidence to establish both, clear and convincing. The *animus manendi* must be actual with no *animo revertendi* . . . .
>
> This discussion shows what an important and essential bearing intention has upon domicile. It is always a distinct and material fact to be established. Intention may be proved by acts and by declarations connected with acts, but it is not thus limited when it relates to mental attitude or to a subject governed by choice.

E. The test of intent with respect to a purported new domicile has been stated as "whether the place of habitation is the permanent home of a person, with the range of sentiment, feeling and permanent association with it" (***Matter of Bourne***, 181 Misc 238, 246, 41 NYS2D 336, 343, ***affd*** 293 NY 785; ***see***, ***Matter of Bodfish v. Gallman***, 50 AD2d 457, 378 NYS2d 138, 140). Moves to other states in which permanent residences are established do not necessarily provide clear and convincing evidence of an intent to change one's domicile (***Matter of Zinn v. Tully***, 54 NY2d 713, 442 NYS2d 990). The Court of Appeals articulated the importance of establishing intent, when, in

Matter of Newcomb (***supra***) it stated. "No pretense or deception can be practiced, for the intention must be honest, the action genuine and the evidence to establish both, clear and convincing." Additionally, formal declarations of domicile or principal residence are generally less persuasive in establishing intent than one's "general habit of life" (***see***, ***Matter of Trowbridge's Estate***, 266 NY 283).

F. There is no dispute that in the years prior to 1988, petitioners were domiciliaries and residents of New York. Petitioners argue that, in February of 1988, they made the decision to abandon their New York domicile and establish Vermont as their domicile. However, they contend that they waited until the end of their children's school term, June of 1988, to actually move to the Moretown,Vermont home which they had acquired in 1985. They assert that beginning in September 1988 their children were registered in and began attending public school in Moretown, Vermont as permanent residents. Petitioners contend that the documentary evidence which they submitted clearly shows that they intended to and did change their domicile to Vermont in June of 1988.

I do not find that the documentary evidence supports a June of 1988 change of domicile as petitioners argue. While the documents submitted do reflect a change of address to Moretown, Vermont, I do not find that evidence sufficient to support a change of domicile in June of 1988 as petitioners argue. Moreover, the bulk of the checks submitted for the period commencing with the end of June 1988 reflect the payment of expenses which would be incurred whether or not petitioners had changed their domicile. However, it is clear from the record that petitioners changed their domicile in September of 1988. Petitioners' intent to change their domicile is clearly reflected in their actions regarding their children's health and education. In September of 1988, petitioners consulted with a Vermont physician for their children's healthcare. Additionally, in the fall of 1988,

petitioners' children were enrolled in and began attending public school in Moretown, Vermont. It is clear that, at that time, Moretown, Vermont became the center of petitioners' life and a change of domicile occurred.

Based on a review of the record in this matter, petitioners have proven by clear and convincing evidence that they changed their domicile from New York to Vermont in September of 1988.

G. Although it has been determined that petitioner changed their domicile from New York to Vermont, they would be properly assessed herein if they both maintained a permanent place of abode in New York and spent in the aggregate more than 183 days there during the year in issue (Tax Law § 605 [b][1][B]).

Petitioners do not dispute that prior to June of 1988, the Armonk property was their permanent place of abode. They argue that they did not utilize the Armonk property from June 1988 until it was sold on December 23, 1988. They do admit that they continued to maintain the utilities, but argue that was done in order for the house to be "shown." Petitioners argument is without merit, they continued to maintain their Armonk, New York home until its sale on December 23, 1988. The Armonk, New York home is a permanent place of abode within the meaning of 20 NYCRR former 102.2(e)(1) (***see***, ***Matter of Evans***, Tax Appeals Tribunal, June 18, 1992, ***confirmed*** 199 AD2d 840, 606 NYS2d 404).

The remaining issue is whether petitioners spent in the aggregate more than 183 days of the taxable year in New York. Petitioners have the burden of proving by clear and convincing evidence that they did not spend more than 183 days in New York during the year in issue (***Matter of Smith v. State Tax Commn.***, 68 AD2d 993, 414 NYS2d 803; ***Matter of Kornblum v. Tax Appeals Tribunal***, 194 AD2d 882, 599 NYS2d 158; ***see also*** 20 NYCRR former 102.2[c]). I find that petitioners have failed to sustain their burden.

Petitioners were under the obligation to maintain "adequate records to substantiate the fact that they did not spend more than 183 days of such taxable year within New York State" (20 NYCRR former 102.2[c]). Petitioners did not submit any proof on this issue even though it was presented by the auditor, as well as in the Division's answer to the petition. Based on the record before me, I am unable to determine how many days petitioners spent in New York in 1988. Petitioners have failed to meet their burden of proof on this issue.

H. During the period in issue, Tax Law former § 638(c) provided, in pertinent part, that

> (1) If an individual changes his status from resident to nonresident he shall, regardless of his method of accounting, accrue to the portion of the taxable year prior to such change of status any items of income, gain, loss or deduction accruing prior to the change of status, if not otherwise properly entering into his federal adjusted gross income for such portion of the taxable year or a prior taxable year under his method of accounting.
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> * * *
>
> (3) No item of income, gain, loss or deduction which is accrued under this subsection shall be taken into account in determining New York adjusted gross income or New York source income for any subsequent taxable period.
>
> (4) The accruals under this subsection shall not be required if the individual files with the tax commission a bond or other security acceptable to the tax commission, conditioned upon the inclusion of amounts accruable under this subsection in New York adjusted gross income or New York source income for one or more subsequent taxable years as if the individual had not changed his resident status.

I. The regulations under 20 NYCRR former 148.10(a) stated, in pertinent part:

> Where the resident status of an individual . . . changes from resident to nonresident, such individual . . . must, regardless of the method of accounting normally employed, accrue and include, on the New York State income tax return and any schedule require [sic] to be filed with such return for the portion of the year prior to the change of resident status, any items of income, gain, loss or deduction (and any New York items of tax preference) accruing prior to the change of residence, if not otherwise properly includible or allowable for New York State income tax purposes or New York State minimum income tax purposes for such portion of the taxable year or for a prior taxable year. That is, in computing New York State taxable income, New York personal service taxable income and New

> York State minimum taxable income for the resident period, such individual. . . must include all items required to be included if a Federal income tax return were being filed for the same period on the accrual basis, together with any other accruals such as deferred gain on installment obligations which are not otherwise includible or deductible for Federal or New York State income tax purposes or for Federal or New York State minimum income tax purposes either for such resident period or for a prior taxable period . . . .
>
> (b)(1) For example, if an individual sells his business at a gain, under contract whereby the purchase price is to be paid in installments and later changes his status from resident to nonresident, he must accrue, on the New York State personal income tax return for the resident period, the entire amount of the gain remaining unpaid from such installment obligations, regardless of the method of accounting he normally uses in reporting his transactions. Furthermore, any long-term capital gain which he realized as a result of the installment sale would also be required to be accrued and taken into consideration in determining the New York items of tax preference to be included in computing the New York State minimum income tax on the *New York State Minimum Income Tax Computation Schedule*, which is required to be filed for the New York State resident period if the New York items of tax preference exceed the allowable specific deduction.

J. Pursuant to Tax Law former § 638(c), the Division accrued as deferred payments amounts received by petitioners from CRP in 1989 and 1990 to the resident part of 1988. The Division also included as additional income the Federal adjusted gross income reported on petitioners' 1988 New York income tax return. Petitioners argue that they properly reported their share of CRP's liquidation of its interest in MP on their 1986 income tax return. They further argue that CRP continued to operate its business after the 1986 transaction and that MP continued to be one of its clients. They argue that the amount they received each year from CRP represents their distributive share of CRP's income, not guaranteed payments from an installment sale. Furthermore, they assert that CRP did not maintain offices in New York after November 1987. Petitioners argue that during 1988, 1989 and 1990, CRP performed all of its work in Oregon, Connecticut and Vermont.

Petitioners arguments are without merit. The handwritten agreement between MP and CRP clearly states that CRP is selling its 10% partnership interest in MP back to MP for $4,000,000.00,

and that the purchase price was to be paid as guaranteed payments deferred over time. In addition, CRP was relinquishing its interest in CRI, a New York corporation, as part of this transaction. Moreover, the 1988 Schedule K-1 issued by MP to CRP specifically identifies the payments as guaranteed. As to petitioners' assertion that CRP continued its business operations after the 1986 transaction, they have failed to present any evidence in support of that assertion (Tax Law § 689[e]). Specifically they have failed to produce any employment agreements between CRP and any entities, including the MP partnership.

The Division properly accrued the deferred payments which petitioners received in 1989 and 1990 in the year 1988, the last year that petitioners were residents of New York.

K. While I have found that the Division's accrual of petitioners' share of the MP guaranteed payments received in 1989 and 1990 to the year 1988 was proper, the amount accrued is incorrect. The Division, in its brief, stated that the deferred payments of $532,022.00 received in 1989 and $145,327.00 received in 1990 were treated as additional New York income in 1988. The Division incorrectly used the total partnership and S corporation income from petitioners' 1990 Schedule E; rather than $132,593.00, the amount which petitioners reported as partnership income from CRP on their Schedule E. In addition to using an incorrect figure in its computation of tax, the Division failed to subtract from the Federal adjusted gross income amount of $646,022.00, the taxable refund of New York State income tax in the amount of $7,877.00 (***see***, Tax Law § 612[c][7]).

Based on the foregoing, the Division is directed to recompute petitioners' 1988 New York State adjusted gross income, as well as the New York State taxable income and the tax due in this matter.

L. Since petitioners have been determined to be New York State residents for tax purposes, the issue of whether certain income payments received in 1988 should be allocated to New York as

New York source income has been rendered moot and will not be addressed.

M. Tax Law § 685(a)(1)(A) states that:

> [i]n case of failure to file a tax return under this article on or before the prescribed date (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not due to willful neglect, there shall be added to the amount required to be shown as tax on such return five percent of the amount of such tax if the failure is for not more than one month, with an additional five percent for each additional month or fraction thereof during which such failure continues, not exceeding twenty-five percent in the aggregate.

Tax Law § 685(b)(1) states that "[i]f any part of a deficiency is due to negligence or intentional disregard of this article or rules or regulations hereunder (but without intent to defraud), there shall be added to the tax an amount equal to five percent of the deficiency."

N. Petitioners have been assessed penalties pursuant to Tax Law § 685(a)(1), for failure to file a tax return for the year 1988 with the State of New York and Tax Law § 685(b) for negligence. Petitioners bear the burden of proving that the failure to file was due to reasonable cause and not due to negligence (Tax Law § 685[b]; § 689[e]). Petitioners have failed to submit any evidence to establish reasonable cause for the waiver of penalties assessed by the Division in the Notice of Deficiency. In their brief, petitioners argue that their tax professional did not intend to misstate income. Reliance upon the advice of a tax professional is not sufficient to prove that petitioners' failure to file a return was not negligent (***see***, ***Matter of Hull***, Tax Appeals Tribunal, December 8, 1994; ***Matter of Etheredge***, Tax Appeals Tribunal, July 26, 1990). Petitioners have failed to sustain their burden of proof. As for petitioners' argument that they may have overstated their 1989 Federal income, whether or not they may have overstated their 1989 Federal income is totally irrelevant to the issue of whether reasonable cause exists to justify the abatement of penalties assessed by New York State for the year 1988.

The Division properly assessed the penalties.

With regard to the interest assessed in this matter, it is noted that the Commissioner of Taxation and Finance has no authority to waive the interest imposed on personal income tax liabilities under Tax Law § 684 (***Matter of Chase***, State Tax Commission, August 12, 1987). The purpose of interest is not to penalize the taxpayer but to reimburse the State for the use of the money (***Matter of Framapac Delicatessen***, Tax Appeals Tribunal, July 17, 1993; ***Matter of Rizzo***, Tax Appeals Tribunal, May 13, 1993).

Essentially, failure to remit tax gives the taxpayer the use of funds which do not belong to him or her, and deprives the State of funds which belong to it. Interest is imposed on outstanding amounts of tax due to compensate the State for its inability to use the funds and to encourage timely remittance of tax due (***Matter of Rizzo***, ***supra***).

O. The petition of Norman and Enid Schibuk is granted to the extent indicated in Conclusion of Law "K" and in all other respects is denied. Notice of Deficiency (Notice Number L-008602436-9) is to be modified in accordance with Conclusion of Law "K" and in all other respects is sustained.

DATED: Troy, New York
May 7, 1998

/s/ *Winifred M. Maloney*
ADMINISTRATIVE LAW JUDGE