STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
LOUIS E. AND FLORENCE FRIEDMAN	:	DETERMINATION DTA NO. 818271
for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Years 1994 and 1995.	:	

Petitioners, Louis E. and Florence R. Friedman, 7136 NW 103rd Avenue, Tamarac, Florida 33321, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the years 1994 and 1995.

A hearing was held before Arthur S. Bray, Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on August 23, 2001 at 10:30 A.M. with all briefs to be filed by January 7, 2002. Petitioners appeared by Lloyd W. Winfield, CPA. The Division of Taxation appeared by Barbara G. Billet, Esq. (Barbara J. Russo, Esq., of counsel).

ISSUES

I. Whether wage income received by petitioner Florence R. Friedman, a nonresident, from Lo-Man Outdoor Store, Ltd. was for services performed entirely outside the State of New York and thus, was not properly subject to New York State personal income tax.

II. Whether penalties imposed against petitioners pursuant to Tax Law § 685(b) and (p) should be sustained.

FINDINGS OF FACT

1. Petitioners, Louis E. Friedman and Florence R. Friedman, filed a New York State Nonresident and Part-Year Resident Income Tax Return (Form IT-203) for the years 1994 and 1995. On each return, they indicated that their filing status was "Married filing joint return." On their 1994 return, petitioners reported income from wages, salaries and tips of $106,000.00 and stated that the New York amount of such income was $53,000.00. On their 1995 return, petitioners reported income from wages, salaries and tips of $104,000.00 and stated that the New York amount of such income was $52,000.00. Petitioners listed their address on each of these returns as 7136 Northwest 103rd Ave., Tamarac, Florida 33321 and indicated on the 1994 return, by checking the "no" box at item "G" on the face of the return, that they did not maintain living quarters in New York State. Petitioners never amended their 1994 return. On the 1995 return, petitioners checked the "yes" box at item "G" thereby indicating that they did maintain living quarters in New York State.

2. Wage and tax statements, for each petitioner, were attached to their returns, indicating that petitioners' employer was Lo-Man Outdoor Store, Ltd. ("Lo-Man"), located in Babylon, New York, and that Mr. and Mrs. Friedman each received wage income of $53,000.00 for 1994 (totaling $106,000.00 as reported), and $52,000.00 each for 1995 (totaling $104,000.00 as reported). These statements also indicate that Federal and New York State personal income tax, Social Security tax and Medicare tax were withheld from petitioners' wages for each year.

3. For 1994, petitioners' return included an attachment which presented a schedule by which each petitioner allocated to New York State a portion of his or her reported wage income from Lo-Man, as follows:

	1994
Total days in year	365
Nonworking days[1]	(123)
Days worked	242
Days worked outside of New York State	(121)
Days worked in New York State	121

4. Petitioners used the foregoing ratio of days worked in New York State to total days worked in each year, as determined by the foregoing schedule, as the basis for allocating a portion of their reported wage income to New York, as follows:

Petitioner	Year	Wage Amount	Allocation Ratio	Wages Allocated
Louis R. Friedman	1994	$53,000.00	121/242	$26,500.00
Florence E. Friedman	1994	53,000.00	120/242	26,500.00
		$106,000.00		$53,000.00

5. Although petitioners prepared a schedule which disclosed the number of days worked within and without New York in 1995, they allocated 100 percent of Mr. Friedman's wages to New York on their return for 1995 on the premise that the work performed by Mr. Friedman in Florida was not for the necessity of the employer and that, for a portion of the year, Mr. Friedman worked in New York. They did not allocate any of Mrs. Friedman's wages to New York for 1995 on the basis that she did not perform any services for Lo-Man in New York during that year.

6. The wages which Lo-Man paid to petitioners were reported as a deduction on the corporation's Federal income tax return. On its franchise tax returns, Lo-Man allocated all of its income to New York.

[1] For 1994, nonworking days consisted of 104 Saturdays and Sundays, 10 holidays and 9 vacation days.

7. The Division of Taxation ("Division") issued a Statement of Audit Changes, dated April 14, 1999, which to the extent at issue, stated that the days petitioners worked at home in Florida for Lo-Man Outdoor Store, Ltd. were considered New York work days. Hence, all of petitioners' wage income was allocable to New York. The Division issued a Notice of Deficiency, dated December 10, 1999, which asserted a deficiency of New York State personal income tax for the years 1994 and 1995 in the amount of $7,648.50 plus interest in the amount of $2,811.36 and penalty in the amount of $2,623.59 for a balance due of $13,083.45. The penalties were assessed for negligence (Tax Law § 685[b]) and for substantial understatement of liability (Tax Law § 685[p]).

8. Prior to the years at issue in this matter, the Division conducted an audit of petitioners' returns for the years 1992 and 1993. This audit initially focused on whether petitioners were properly taxable as nonresidents of New York. Petitioners spent time in New York each year and, contrary to the information on the face of their returns, maintained a home in Bay Shore, New York. After examination, the auditor nonetheless concluded that petitioners, who had moved to Florida in or about 1981, were Florida domiciliaries and spent fewer than 183 days per year in New York State. Accordingly, petitioners were found to be properly taxable as nonresidents of New York. However, the auditor noted that petitioners continued to own Lo-Man, received wage income from such business, and reported that a portion of the wage income was allocable to and taxable by New York State on the basis of the number of days worked in New York State over the total number of days worked in each year. Since there was no evidence that petitioners performed services outside of New York State of necessity in the service of their employer rather than for their own convenience, the auditor concluded that all of petitioners' wage income was properly subject to tax by New York State. This conclusion prompted the

Division to issue a Notice of Deficiency to petitioners which asserted a deficiency of personal income tax. Petitioners, in turn, filed a petition for a hearing challenging the Notice of Deficiency. Petitioners did not prevail before the Division of Tax Appeals and pursued an appeal before the Tax Appeals Tribunal.

9. ***In Matter of Louis E. and Florence R. Friedman*** (Tax Appeals Tribunal, March 2, 2000) the Tribunal noted that the Administrative Law Judge accepted petitioners' concession that the wage income paid by Lo-Man to Mr. Friedman was fully taxable by New York State because he performed services for Lo-Man both within and without New York State, and the services performed for Lo-Man in Florida were executed for the convenience of Mr. Friedman and not for the necessity of Lo-Man. The Tribunal also noted that the Administrative Law Judge also found that Mrs. Friedman's income was fully allocable to and taxable by New York State. In reaching this conclusion, it was pointed out that any allocation of income must be based on a showing that Mrs. Friedman performed services for her employer at her home in Florida out of necessity rather than convenience. The Administrative Law Judge determined that Mrs. Friedman performed no discernable services other than holding corporate office and being available for consultation either within or without New York. Therefore, Mrs. Friedman could not apportion any of her compensation from Lo-Man to Florida. After reviewing the determination of the Administrative Law Judge, the Tribunal concluded that "the Administrative Law Judge completely and adequately addressed the issues presented to him and correctly applied the Tax Law and relevant case law to the facts of this case." (***Id.***)

10. During the years in issue, petitioners maintained a home in New York and a home in Tamarac, Florida. During the same period of time, each petitioner was an officer and 50 percent

shareholder of Lo-Man. Lo-Man was an "outdoor store" which sold clothing, footwear and various types of apparel at the retail level.

11. Prior to her retirement, which was in approximately 1980, Mrs. Friedman worked at the store performing duties in the office, working on the floor and ringing up sales at the cash register.

12. During the years in issue, petitioners would come to New York in or around June and leave in the beginning of September. They would return to New York for a period of time on or around Thanksgiving. When petitioners were in New York, Mr. Friedman went to his office in the store where he would look through brochures and check with his manager about decisions that had to be made regarding personnel or items that should be purchased. Mrs. Friedman never accompanied Mr. Friedman when he went to the store and, when she was in New York, Mrs. Friedman only went to the store to visit with the employees. Mrs. Friedman considered herself to be on vacation when she was in New York and, during these periods, she was involved with her children and grandchildren.

13. When petitioners were in Florida, Mr. Friedman would call the store to give the secretary-bookkeeper of Lo-Man instructions on what to do. If the secretary-bookkeeper encountered a problem, she would call and speak to Mr. Friedman about how to proceed. If Mrs. Friedman answered the telephone, the call would be transferred to Mr. Friedman.

14. Mrs. Friedman has a college degree from New York University in personnel and industrial relations. Certain questions pertaining to the business arose each year. Lo-Man's accountant made a practice of conferring with Mrs. Friedman on questions involving the pension plan. These concerns were only addressed when Mrs. Friedman was in Florida because

employee records, financial statements regarding investments and documentation from the pension company were kept at an office maintained by Mrs. Friedman at her home in Florida.

15. When petitioners are in Florida, they receive a weekly package that has Lo-Man's cash register tapes, bank statements, documents pertaining to inventory and correspondence that was sent to the store. Mrs. Friedman reviews each cash register tape. Thereafter, Mr. and Mrs. Friedman confer regarding what items are selling and whether to discount certain items. At the end of the fiscal year, they also confer on how the business did for the year, what they should do with their assets and how much money they should set aside for a poor season.

16. When petitioners were in New York, they did not visit Lo-Man's accountant at his office. It was Mr. Friedman's practice to confer with his accountant over lunch at a restaurant. The accountant never saw Mrs. Friedman outside of his office when she was in New York.

SUMMARY OF THE PARTIES' POSITIONS

17. At the hearing, petitioners' accountant explained that the allocation of petitioners' wages in 1994 was purely arbitrary. On the basis of petitioners' position that Mrs. Friedman did not perform any work in New York, petitioners submit that the allocation of wages in 1994 should have been the same as that reported in 1995, that is, 100 percent of Mr. Friedman's wages were allocable to New York and none of Mrs. Friedman's wages were subject to New York State personal income tax. Petitioners contend that the convenience of the employer test does not apply to the wages received by Mrs. Friedman because Mrs. Friedman did not perform any work in New York. Petitioners also maintain that since Mrs. Friedman is an officer and shareholder she does not have to justify the amount of salary that she received. Petitioners also contend that the tax returns were prepared using a computer and that, inadvertently, a box on the input sheet was not checked. As a result, the New York State income tax return for 1994 did not

indicate that petitioners had a home in New York. Petitioners contend that there was no intent to indicate that petitioners did not have a home in New York. In this regard, petitioners note that their income tax return for 1995 indicates that they have a residence in New York. In a posthearing letter, petitioners reiterate their position that none of Mrs. Friedman's income is allocable to New York because she did not perform any services in New York.

18. In its letter brief, the Division notes that the Tax Appeals Tribunal determined that for the years 1992 and 1993, 100 percent of petitioners' income should be allocated to New York. In its answer, the Division submitted that the doctrines of collateral estoppel and res judicata should apply to the Tribunal's decision. The Division also points out that petitioners were audited for years prior to 1992 which resulted in the Division's reallocating all of petitioners' wage income to New York. The Division points out that this audit result was conceded and the tax deficiency was paid.

The Division notes that Lo-Man allocates 100 percent of its income to New York and that Mr. Friedman allocates the same percentage of his wages to New York. The Division then argues that Mrs. Friedman could not recall any specifics about the services she performed in Florida and that if an emergency situation arose while petitioners were in New York, Mr. Friedman would consult with Mrs. Friedman about it. Similar testimony was offered by the accountant. The Division posits that there has been no showing that the prior years were different from the current years and that even if there were consultations in Florida, there has been no proof that it was due to the necessity of Lo-Man.

Lastly, the Division argues that petitioners have failed to establish reasonable cause for the abatement of penalties. In this regard, the Division points out that the Tribunal found against petitioners and petitioners have admitted that their circumstances have not changed. Further,

petitioners indicated on their 1994 return that they did not maintain living quarters in New York even though they had a home in New York. The Division then points out that petitioners checked the "No" box in the years at issue before the Tribunal and made no attempt to amend their 1994 return.

CONCLUSIONS OF LAW

A. Tax Law § 631(a) provides, in part, that "[t]he New York source income of a nonresident individual shall be the sum of the following: (1) the net amount of items of income, gain, loss and deduction entering into his federal adjusted gross income, as defined in the laws of the United States for the taxable year, derived from or connected with New York sources. . . ." To the extent in issue, the Tax Law defines the phrase "[i]tems of income, gain, loss and deduction derived from or connected with New York sources" as those which are attributable to "a business, trade, or profession or occupation carried on in this state. . . ." (Tax Law § 631[b][1][B].) The Commissioner's regulations at 20 NYCRR 132.18(a) provide, in part, that:

> If a nonresident employee . . . performs services for his employer both within and without New York State, his income derived from New York State sources includes that proportion of his 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 working days employed both within and without New York State. . . . However, any allowance claimed for days worked outside of New York State must be based upon the performance of services which of necessity, as distinguished from convenience, obligate the employee to out-of-state duties in the service of his employer.

Petitioners' representative has accurately noted that there is an important caveat to the rule set forth above. A nonresident who performs no work within the State of New York is not subject to New York State personal income tax on the wages received from said employment (***Matter of Linsley v. Gallman,*** 38 AD2d 367, 329 NYS2d 486, ***affd*** 33 NY2d 863, 352 NYS2d 199; ***Matter of Gleason v. State Tax Commn.,*** 76 AD2d 1035, 429 NYS2d 314; ***Matter of***

Hayes v State Tax Commn., 61 AD2d 62, 401 NYS2d 876) regardless of the fact that the payment may be made from a location within New York or that the employer is, as here, a resident corporation (***see***, 20 NYCRR 132.4[b]).

B. The Division first points to the fact that, in a prior decision, the Tribunal determined that, for the years 1992 and 1993, 100 percent of petitioners' income should be allocated to New York. (***Matter of Friedman, supra.***) As noted earlier, in its answer the Division submitted that the doctrines of collateral estoppel and res judicata should apply to the Tribunal's decision. The Division also notes that petitioners agreed to the audit findings for years prior to 1992 and submits that petitioners have acknowledged that their working situation has not changed from the years 1992 and 1993 to the years currently in issue.

C. The foregoing arguments by the Division are without merit. There is no question that, where the relevant facts are the same, the decisions of the Tax Appeals Tribunal constitute binding precedent on matters pending before the Division of Tax Appeals (***see***, Tax Law § 2006[7]). However, the inquiry does not end here. It is well established that the principle of res judicata is not applicable when a subsequent proceeding involves the liability of a different taxable year (***see, Commr. v. Sunnen***, 333 US 591, 92 L Ed 898). Further, although there appears to be a difference of opinion within the Federal courts, it is concluded that the better position is that collateral estoppel does not apply to recurring factual situations which may change from time to time (***see, e.g.***, ***Hersloff v. Commr.***, 46 TC 545). Here, there is a critical difference between the record concerning the years 1992 and 1993 and the record in this matter. In the record before the Tribunal there was no evidence that Mrs. Friedman had any discernable duties. Consequently, there was no basis for the conclusion that Mrs. Friedman was "working" in Florida for the necessity of her employer. Petitioners' reluctance to explain Mrs. Friedman's

duties was apparently based on petitioners' belief that, as an officer and stockholder, Mrs. Friedman did not need to justify her salary. However, this was not the point. It was necessary to identify Mrs. Friedman's duties in order to analyze the question of whether Mrs. Friedman was working in Florida for the necessity of her employer. As the hearing in this matter progressed, it became clear that Mrs. Friedman regularly conferred with Mr. Friedman and the business's accountant on Lo-Man's pension plan. In addition, Mrs. Friedman analyzed Lo-Man's cash register tapes and conferred with Mr. Friedman on what items were selling and whether certain items should be discounted. This testimony distinguishes this case from the prior proceeding.

D. Contrary to the Division's argument, Mr. Friedman's testimony that Mrs. Friedman's working circumstances did not change from 1992 and 1993 to the years in issue does not support the Division's position. This testimony merely reflects Mr. Friedman's belief that they should have prevailed in the earlier matter. Lastly, petitioners' agreement to pay the tax for the years prior to 1992 cannot be interpreted as a concession by petitioners that they would not question the Division's position in any subsequent year.

E. In support of its position that Mrs. Friedman should have allocated 100 percent of her wages to New York, the Division notes that Lo-Man allocates 100 percent of its income to New York. This argument is rejected because it is contrary to the Commissioner's regulations which provides, in part, that "Compensation for personal services rendered by a nonresident individual wholly without New York State is not included in his New York adjusted gross income, regardless of the fact that payment may be made from a point within New York State or that the employer is a resident individual, partnership or corporation." (20 NYCRR 132.4[b].)

F. The Division's argument that petitioner's testimony was vague and lacking specifics is rejected. As the hearing progressed, Mrs. Friedman's testimony became sufficiently detailed

to establish that she performed services for Lo-Man in Florida and not in New York. Moreover, the fact that Mr. Friedman was allocating 100 percent of his wages to New York has no bearing on whether Mrs. Friedman was required to do the same. It follows that since Mrs. Friedman did not perform any services for Lo-Man in New York, her wages were not subject to New York State personal income tax.

G. The remaining issue is whether there is reasonable cause for the abatement of penalties. For the year 1994, petitioners conceded that they did not properly allocate Mr. Friedman's wage income to New York, that he performed services for Lo-Man in New York and that none of the services that he performed for Lo-Man in New York were performed for the necessity of the employer. In addition, petitioners acknowledged that they erroneously failed to check the box showing that they had a residence in New York. Under these circumstances, petitioners have not shown any basis for modifying the penalties asserted for negligence or substantial understatement of liability.

H. For the year 1995, petitioners correctly reported 100 percent of Mr. Friedmans' wage income to New York and none of Mrs. Friedman's wage income to New York. In addition, petitioners' return correctly reported that they maintained a residence in New York. It follows that since the reasons raised by the Division to impose penalties are without merit, the penalties asserted for this year are cancelled.

I. The petition of Louis E. and Florence R. Friedman is granted to the extent of Conclusions of Law "C," "F," and "H" and the Division is directed to modify the Notice of

Deficiency, dated December 10, 1999, accordingly; except as so granted, the petition is in all other respects denied and the Notice of Deficiency is sustained.

DATED: Troy, New York
June 27, 2002

/s/ Arthur S. Bray
ADMINISTRATIVE LAW JUDGE