STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
JOHN AND CAROLINE GOULD	:	DETERMINATION DTA NO. 819897
for Redetermination of a Deficiency or for Refund of New York State and New York City Personal Income Tax under Article 22 of the Tax Law and the New York City Administrative Code for the Years 1998, 1999 and 2000.	:	

Petitioners, John and Caroline Gould, c/o William Lenihan, 10 Park Avenue, #8B, New York, New York 10016, filed a petition for redetermination of a deficiency or for refund of New York State and New York City personal income tax under Article 22 of the Tax Law and the New York City Administrative Code for the years 1998, 1999 and 2000.

A hearing was held before Catherine M. Bennett, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York on March 10, 2005 at 10:30 A.M., with all briefs to be submitted by September 23, 2005, which date commenced the six-month period for the issuance of this determination. Petitioners appeared by William O. Lenihan, Esq. The Division of Taxation appeared by Christopher C. O'Brien, Esq. (Peter B. Ostwald, Esq., of counsel).

ISSUES

I. Whether laches or equitable estoppel should apply in this matter such that the Division of Taxation should be estopped from asserting nonresident income allocation based on days

worked in New York versus days worked out of New York pursuant to a previous agreement made between the Division of Taxation and petitioners.

II. Whether the Division of Taxation properly asserted additional tax against petitioners on their nonresident income earned within New York State for tax years 1998, 1999 and 2000.

III. Whether the Division of Taxation properly included in petitioners' nonresident income allocation to New York, income from the business activities of Mr. Gould's partnership, reported on his Form 1040, Schedule E.

IV. Whether petitioners have properly substantiated an allocation of nonresident income based on days worked in New York State.

FINDINGS OF FACT

1. During the tax years in issue, 1998, 1999 and 2000, John and Caroline Gould[1] were residents of the State of Connecticut, and for many years, nonresidents of New York State. Petitioner John Gould was a limited partner in a partnership doing business in New York State, throughout the United States and worldwide.

2. Petitioner was a limited partner of Midland Paper New York Limited Partnership ("Midland"), a Delaware partnership, whose general partner was Midland Paper Company, an Illinois corporation, headquartered in Chicago. Midland's principal place of business was not provided by petitioner and the partnership agreement submitted post-hearing was missing its Schedule 1, where this information was allegedly specified. It is not established by the record that Midland had an office in New York. However, petitioner's Forms K-1, Partner's Share of

[1] Since the entire assessment concerns income generated by John Gould, and Caroline Gould is a petitioner only by having filed a joint tax return with her husband John, for simplicity, any references herein to "petitioner" shall refer directly to John.

Income, Credits, Deductions, etc., from Midland's Federal partnership return, were issued to "John Gould, c/o Midland Paper NY L.P., 52 Vanberbilt Ave., 14th Fl, New York, NY 10012."

3. Petitioner filed Form IT-203, a Nonresident New York State Income Tax Return, for all years in issue. The only evidence of that filing for 1998 in the record is a computer-generated document produced by the Division of Taxation ("Division"), which gives data from the filed return, the fact that it was filed on August 6, 1999, and the tax calculated. It does not, however, bear attached schedules as to how the income was allocated to New York (sales in New York or days worked in New York). A later amended version of the 1998 Form IT-203 indicates that the original was filed on the income allocation basis of sales in New York to sales everywhere.

The Forms IT-203 filed by petitioner for 1999 and 2000, however, were submitted into evidence in their original filed format, with attached schedules. Both, as originally filed, bear the attachment of Form IT-203-ATT, displaying the calculation of the allocation of income to New York on the basis of days worked in New York compared to total days worked. Both returns were signed by Mr. Lenihan, petitioner's current representative, as a paid preparer, and filed July 15, 2000 and June 10, 2001, respectively, under extension. The allocation schedules follow:

	1999	2000
Total Days	365	365
Saturdays and Sundays not worked	104	104
Holidays not worked	10	10
Vacation	20	20
Total non-working days	134	134
Total days worked in year at this job	231	231
Total days included [above] worked outside New York	169	169

Days worked in New York State	62	[illegible]

4. In October 2001, the Division initiated an audit examination of petitioner's personal income tax returns to determine the proper New York income allocation for each of the three tax years at issue. On numerous occasions throughout the audit, the Division requested substantiation of petitioner's New York income allocation. Petitioner and his representative, William Lenihan, Esq., failed to furnish documents requested by the Division in the early part of the audit, and repeatedly denied the Division access to photocopy pertinent records requested by the auditor. Based upon petitioner's failure to substantiate the claimed New York income allocation, the Division disallowed the allocation of wages, Schedule E and Schedule C income, and all sources of petitioners' income were deemed New York sources.

5. The Division issued to petitioners a Statement of Personal Income Tax Audit Changes dated September 27, 2002, detailing its computation of the asserted tax liability for the three years in issue. On the statement appeared the following: "Since, you failed to substantiate an allocation of income at audit, we are issuing the proposed statement of audit adjustments sourcing all income to New York State and City."

6. Petitioners had executed a Consent Extending the Period of Limitation for Assessment of Personal Income Tax for the period ending December 31, 1998 until December 31, 2002.

7. The Division thereafter issued to petitioners, John M. and Caroline Gould, a Notice of Deficiency dated October 28, 2002, assessing New York State and New York City personal income tax in the amounts of $56,800.58 and 2,589.49, plus penalty and interest for the year 1998; $34,554.44 and $444.57, plus penalty and interest for the year 1999; and $16,087.45 plus penalty and interest for the year 2000.

8. Petitioner appeared only by his representative, Mr. Lenihan, at the hearing and no affidavit by petitioner was presented. Throughout the entire hearing process, petitioner's representative repeatedly stated that the Division has failed to provide petitioner with the information he requested under the Freedom of Information Law ("FOIL") in seven requests which concerned the same issues in prior audits of this petitioner between 1989 and 1995. Mr. Lenihan was present as petitioner's representative in four or five previous audits conducted by the Division for those years. When asked what other documentation he had from representing petitioner on those prior audits that may shed some light on current issues raised, Mr. Lenihan stated, "That's all I want to submit at this time." (Tr. p.46.) The following statement in the petition in this matter explains petitioner's position:

> The New York State Tax Department, Audit Division determined in an early audit that taxpayers [sic] income allocated to New York should be based on a percent of sales in New York over sales nationwide. They compiled this formula of allocating by sales versus the usual computation based on days worked in the State. The income subject to this allocation was also direct income received by taxpayer and did not include equity reserves. Two subsequent audits by New York State followed both of these formulas and resulted in 'No Changes'. New York State will not furnish any information relating to the above three audits or the two formulas that they created.

9. Petitioners' representative made numerous FOIL requests for their previous personal income tax audits for tax years 1988, 1989 and 1995. Specifically, he was in search of an agreement he believes existed between petitioner and New York State, initiated by the Division, which governed how petitioner filed his returns for the past approximately 18 years, and should dictate the allocation of income to New York in this case, utilizing the method of sales in New York to total sales for reporting purposes.

10. At one point the FOIL records access office responded to petitioner with the following information:

I have been advised of the following status of these two audits:

- X-367641010 (1989-1992): this audit involved non-resident New York wages, resulted in a very small adjustment, and was closed by the Suffolk District Office; there are no materials available.

- X-677816193 (1995): attached is a copy of the purged audit case information showing that this case was closed as a 'no change' audit; there are no other materials available.

11. Petitioner submitted an "Amended and Restated Agreement of Limited Partnership of Midland Paper New York Limited Partnership" post-hearing. Petitioner's name did not appear on the agreement, and the signature page and Schedule A, bearing a list of partners, addresses and percentage interests, were missing from the submission. Additionally, two pages of pertinent information concerning cash distributions and allocation of profits and losses, Article IV of the partnership agreement, were omitted from the submission.

12. Petitioner submitted his Schedules K-1, Partner's Share of Income, Credits, Deductions, etc., from Form 1065, the US Partnership Tax Return of Midland, for tax years 1998, 1999 and 2000. The partner was listed as John Gould, with an address "c/o Midland Paper NY L.P., 52 Vanderbilt Ave., 14th Fl, New York, NY 10012," and a social security number which coincides with petitioner's own Federal tax return. It shows petitioner as a limited partner with a profit sharing, loss sharing, and ownership of capital percentage for 1998 and 1999 of 23.02%, and 22.33% for 2000. The K-1's for 1998 and 1999 listed the percentages as "before change or termination" rather than at "end of year" as did the K-1 for tax year 2000, which was the final K-1. The financial information reported by each of the Schedules K-1, is set forth below:

K-1 Distributive Share Item (Line No.)	1998	1999	2000
Ordinary Income (loss) from trade or business activities (1)	$297,950.00	$215,691.00	$119,503.00
Guaranteed payments to partner (5)	$770,588.00	$476,236.00	$236,677.00
Net section 1231 gain (loss) (6)		($901.00)	
Charitable contributions (8)	$771.00		$232.00
Net earnings from self employment (15a)	$770,588.00	$476,236.00	$236,677.00
Gross nonfarm income (15c)	$770,588.00	$476,236.00	$236,677.00
Depreciation Adjustment on property placed in service after 1986 (16a)	$573.00	($165.00)	($434.00)
Adjusted gain or loss		($338.00)	
Nondeductible expenses (21)	$1,621.00	$2,794.00	$1,233.00
Distributions of money (22)	$148,043.00	$100,300.00	$890,015.00
Capital account at beginning of year	$568,274.00	$700,874.00	$801,175.00
Capital contributed during the year			
Partner's share of lines 3, 4, and 7, Form 1065, Schedule M-2	$280,643.00	$200,601.00	$88,840.00
Withdrawals and distributions	$148,043.00	$100,300.00	$890,015.00
Capital account at end of year	$700,874.00	$801,175.00	0.00

Each year the amount of the ordinary income (from line 1) was reported on petitioner's Form 1040, Schedule E, as partnership income, and the amount of guaranteed payments (from line 5) was reported on petitioner's Form 1040, Schedule C, as gross sales or receipts from sales (as the principal business activity).

13. New York partnership allocation percentages or schedules for each tax year were not made part of the record. There is no evidence of whether a New York Partnership Tax Return was filed by Midland.

14. Petitioner filed amended Forms IT-203 after the conclusion of the Division's audit stating he was doing so to satisfy the Division's request for petitioner to file on an allocation basis using days worked in New York/total days. Mr. Lenihan signed each of the amended returns as paid preparer in early November 2003. The allocation schedules as filed with the amended returns follow:

	1998	1999	2000
Total Days	365	365	365
Saturdays and Sundays not worked	104	104	104
Holidays not worked	10	10	10
Vacation	20	20	20
Total non-working days	134	134	134
Total days worked in year at this job	231	231	231
Total days included [above] worked outside New York	199	202	200
Days worked in New York State	32	29	31

15. In advance of the hearing, Mr. Lenihan reviewed petitioner's diaries with him and entered notations into petitioner's diaries which he believed would support petitioner's allocation of days worked in New York and elsewhere. Mr. Lenihan identified which handwriting represented his notations. Next to or below the entries made by petitioner, Mr. Lenihan often re-wrote the name of the person petitioner was meeting, a company name and the state in which the meeting took place. Many midweek pages of petitioner's diaries bore no entries. When summarized numerically, Mr. Lenihan counted blank diary pages as non-New York work days. He photocopied the diary information and submitted it to the Division for review by auditor Henrietta Lubkowski. The schedules prepared by Mr. Lenihan and submitted at hearing showed the following day count:

	1998	1999	2000
Total Days	365	365	365
Total non-working days	116	120	123
Total working days	249	245	243
Total days worked outside New York	169	174	189
Days worked in New York State	80	71	54

16. The Division submitted the affidavit of the auditor Henrietta Lubkowski post-hearing, having received permission from the Administrative Law Judge at the hearing to make such submission. In pertinent part, her conclusion was that petitioner had failed to properly substantiate his claimed New York income allocation based upon the number of days he worked in and out of New York, resulting in the issuance of a notice of deficiency which reflected in a 100% allocation of income to New York. Ms. Lubkowski performed a review and analysis of petitioner's 1998, 1999 and 2000 diaries and concluded that the records did not appear to be contemporaneous, were not in valid format, were not accompanied by supporting documentation and were thus unreliable. Thus, the Division considered the day count as set forth in Finding of Fact "15" unsubstantiated, and continued to deem all of petitioner's income as from New York sources.

SUMMARY OF THE PARTIES' POSITIONS

17. Petitioner first argues that the doctrines of laches or equitable estoppel should apply to this matter and prevent the Division from now retroactively changing the method of allocating income as a nonresident of New York. Petitioner believes that the Division's course of conduct over approximately 15 years resulted in allowing petitioner to file his nonresident New York

income tax return using a sales in New York/total sales everywhere allocation method, and the Division should be estopped from now asserting a different method.

Petitioner's second point of contention is that the agreement which petitioner claims to have made with the Division regarding the determination of the New York portion of his nonresident income on the basis of sales in New York to sales made everywhere is the method under which the Division should allow petitioner to file.

Petitioner also maintains that the income which he reported on his Form 1040, Schedule E, as partnership income from form K-1, line 1, should not be allocated to New York because it is equity income based on a percentage of the ownership of the partnership, and is not either actively or constructively received by petitioner, and will not be until he dies, is terminated or retires.

Petitioner's final argument is that if the Division requires petitioner to file and compute his nonresident New York income on the basis of days worked in New York/total days worked, then the Division should accept the diaries and American Express records as sufficient substantiation for the summary schedules compiled by petitioner's representative.

18. The Division contends that petitioner has failed to show the applicability of the doctrine of laches or equitable estoppel to this matter.

The Division maintains that petitioner has not shown the existence of any prior agreement between it and petitioner that would dictate the allocation method, and that it has properly determined petitioner's New York income allocation for tax years 1998, 1999 and 2000 based upon days worked in New York/days worked everywhere, in contrast with sales made in New York/sales everywhere.

Finally, the Division argues that petitioner has failed to show by clear and convincing evidence that the notice of deficiency was erroneous or improper.

CONCLUSIONS OF LAW

A. Petitioner first argues that the Division should be estopped from asserting the deficiency on the basis of its conduct over the past 18 years of auditing petitioner. Laches or equitable estoppel, usually referred to simply as estoppel, are not, as a general proposition, available as defenses to governmental acts absent a showing of exceptional facts which require their application to avoid a manifest injustice (***see, Matter of Sheppard-Pollack, Inc. v. Tully***, 64 AD2d 296, 409 NYS2d 847). This rule applies particularly to a taxing authority because sound public policy favors full enforcement of the Tax Law (***Matter of Turner Constr. Co. v. State Tax Commn.***, 57 AD2d 201, 394 NYS2d 78). Exceptions to the doctrine have been rare and limited to unusual fact situations.

The defense of laches requires two important elements: delay and prejudice to a party due to that delay (***see, generally***, 75A NY Jur 2d, Limitations and Laches, §§ 4, 357-370). For petitioner to bar the Division's actions on the ground of laches, he must prove the existence of the following four elements (***id*** at § 364):

(1) Conduct on the part of petitioner that gives rise to a situation for which the Division seeks a remedy. Petitioner was working in New York State as a nonresident partner of a partnership doing business in New York, which conduct gave rise to the question of the proper allocation of nonresident income to New York.

(2) Delay by the Division in asserting the Division's rights, the Division having had knowledge or notice of petitioner's conduct and having been afforded an opportunity to previously assert its rights. This fact has not been established by petitioner. The Division

acquired knowledge of petitioner's nonresident business activities from prior audits. Petitioner asserted throughout the hearing that an agreement existed between the Division and petitioner which set forth an allocation formula. However, this assertion was never supported by any documentation. Petitioner claims to have made seven or more FOIL requests that did not produce any such agreement and he admittedly denied the Division access to his records during a large part of the audit, potentially to his own detriment. Any delay that has been established by the facts has been at petitioner's own hand. The Division timely asserted its rights to review petitioner's allocation of nonresident income formula.

(3) Lack of knowledge or notice to petitioner that the Division would assert the right on which he basis his suit. This fact has not been established by petitioner. The existence of the alleged agreement based on a sales to sales allocation between the Division and petitioner arising from previous audits may have led petitioner to believe that he could continue to allocate in the same manner, barring a change in posture by the Division to allocation based on a days formula. However, petitioner never met his burden of proof that the agreement actually existed or was not more than the result of settlement negotiations for previous years.

(4) Injury or prejudice to petitioner in the event the Division's assessment is upheld or duplicate taxation is paid to the State of Connecticut where petitioner is a resident. This fact has not been established by petitioner. Petitioner cannot claim injury from the assessment issued by the Division when he is required by law to maintain records supportive of his filed tax return. Further, petitioner filed his original nonresident returns on the same basis (at least for 1999 and 2000) as was permitted by the Division, i.e., a days in/days out allocation. Having done so, presumably petitioner then filed his Connecticut returns in conjunction therewith so as not to duplicate the taxation of any income. There is no prejudice to petitioner established herein. Any injury to petitioner based on the New York State assessment or any duplicate taxes paid to

Connecticut, a refund for which may now be unavailable due to the statute of limitations, was brought on by petitioner's own actions.

Accordingly, petitioner has failed to establish that the doctrine of laches should bar the Division from pursuing the assessment against petitioner.

B. The Tax Appeals Tribunal has adopted a three-part test to determine the applicability of equitable estoppel to specific cases. Briefly, the test asks whether petitioner had the right to rely on the Division's representation; if, in fact, there was such reliance and whether the reliance was to the detriment of petitioner (***Matter of AGL Welding Supply Co.***, Tax Appeals Tribunal, May 11, 1995, ***confirmed Matter of AGL Welding Supply Co. v. Commissioner of Taxation & Fin.***, 238 AD2d 734, 656 NYS2d 502, ***lv denied*** 90 NY2d 808, 664 NYS2d 270; ***Matter of Harry's Exxon Serv. Sta.***, Tax Appeals Tribunal, December 6, 1988).

The facts in this case do not rise to the level of "exceptional" which would justify the implementation of the doctrine of equitable estoppel. While petitioner allegedly relied on the representations made to him by the Division, he was not able to produce the agreement upon which he relied, and any detriment he suffered was due to his own failure to follow the letter of the law. Thus, petitioner has also failed to establish that equitable estoppel should bar the Division from pursuing the assessment against petitioner.

C. It is well settled that a nonresident, such as petitioner, is subject to income tax by New York only on such income as is "derived from or connected with New York sources" (Tax Law § 631[a]), including "his distributive share of partnership income, gain, loss and deduction, determined under section six hundred thirty-two" (Tax Law § 631[a][1][A]). Income and deductions derived from or connected with New York sources include those "attributable to a

business, trade, profession or occupation carried on in this state (Tax Law § 631[b][1][B]; 20 NYCRR 132.4[a][2]) .

Tax Law § 632 provides the following guidance on determining the portion of a nonresident partner's income which must be deemed from New York sources:

> (a) Portion derived from New York sources.
>
> (1) In determining New York source 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-one.
>
> * * *
>
> (b) Special rules as to New York sources. In determining the sources of a nonresident partner's income, no effect shall be given to a provision in the partnership agreement which--
>
> (1) characterizes payments to the partner as being for services or for the use of capital, or
>
> (2) allocates to the partner, as income or gain from sources outside New York, a greater proportion of his distributive share of partnership income or gain than the ratio of partnership income or gain from sources outside New York to partnership income or gain from all sources, except as authorized in subsection (d). . .
>
> * * *
>
> (d) Alternate methods. The tax commission may, on application, authorize the use of such other methods of determining a nonresident partner's portion of partnership items derived from or connected with New York sources, and the modifications related thereto, as may be appropriate and equitable, on such terms and conditions as it may require.

A nonresident partner's share of distributive income may include the partner's distributive share, even if it was never received and will likely never be received, and also guaranteed monthly payments that were distributions of partnership income (100 NY Jur 2d, Taxation and Assessment, § 1197).

Simply stated, when a nonresident taxpayer is a member of a partnership which conducts business both within and without New York State, he is taxable on the portion of his net distributive share of partnership income that is apportioned to New York. As a general rule, unlike the earnings received by an employee, a partner's distributive share of partnership income is not allocated in proportion to the number of working days the partner is within and without the State (100 NY Jur 2d, Taxation and Assessment, § 1198). Rather, a partner's distributive share is allocated pursuant to the partnership agreement. A nonresident partner may not allocate his or her distributive share of partnership income to sources within and without the State in any greater proportion than the partnership itself allocated its income. This principle applies even though the partnership makes no out of state allocation, including in those instances where it could have, but determined not to do so (***id***). One exception to the allocation being dictated by the partnership agreement is Tax Law § 632(d), where the Division, upon application, authorizes the use of an alternative method that it deems appropriate under the circumstances. However, although the Division may authorize the use of an alternative method, a method approved for particular years does not constitute an alternative method under Tax Law § 632(d), presumably subject to the notice requirement of due process to effectuate a change in that method, where the Division reserves the right to change the method of reporting for subsequent years (***Matter of Capone***, State Tax Commission, July 9, 1984).

The more specific questions raised by this matter are the following:

1. Did petitioner receive a distributive share of partnership income?
2. How did the partnership allocate income within and without New York State?
3. What does the partnership agreement dictate?
4. Did the Division authorize the use of an alternative method for petitioner to allocate income as a nonresident partner?
5. If an alternative method was authorized, did the Division violate petitioner's due process by changing the method by which petitioner should report its partnership income

retroactively without notice of such change based upon an agreement which was made between the parties in a prior audit?

6. Has petitioner substantiated the method authorized?

D. The meaning of distributive share of partnership income for purposes of Tax Law § 632(a)(1) is determined by the meaning of this phrase in Internal Revenue Code § 704(a), which states that a partner's distributive share is determined by the partnership agreement. If the agreement gives the taxpayer no interest in the partnership's income or losses, then one may conclude that the taxpayer has no interest in the partnership, and did not receive a distributive share (***see, Matter of Kyle***, Tax Appeals Tribunal, May 18, 1995). In this case, the partnership agreement was submitted with missing pages, particularly the section which addresses cash distributions and allocation of profits and losses. Thus, I am not able to determine what the partnership agreement dictated as to whether and to what extent petitioner had a distributive share from the partnership. However, two other items in the record lend information to allow a determination. The Schedules K-1, Partner's Share of Income, Credits, Deductions, etc., filed with a US Partnership Tax Return, Form 1065, and submitted into the record, were presumably prepared and filed in accordance with the terms of the partnership agreement. The K-1's for all years in issue indicate petitioner had profit and loss sharing percentages and distributive items of income specified in Finding of Fact "12". In addition, Mr. Lenihan's post-hearing brief references Tax Law §§ 631 and 632 and discusses the allocation of a partner's distributive share without denying its receipt by petitioner. As to the guaranteed payments, reported by petitioner as Schedule C gross income, petitioner argues only about the method of allocation to New York, not the characterization of the payment. As to the ordinary income from the partnership's business activities (Schedule K-1, line 1), petitioner argues that previous audits deemed this as not reportable to New York until it was distributed, since there was no active or constructive

receipt during the years in issue. Unfortunately, with the incomplete partnership agreement and no additional supporting documentation, I cannot reach the same conclusion, and petitioner has not met his burden of proof that this too is not a distributive share of partnership income, allocable to New York State. Thus, the K-1 items in issue, the guaranteed payments and the ordinary income from business activities, reported as distributive share items thereon, are deemed distributive share items, subject to allocation to New York.

Concerning how the partnership allocated New York income to its partners, the partnership return and the partnership agreement are required to set forth such information (20 NYCRR 158.9[a]; IRC § 704[a]). No New York partnership tax return for Midland was provided, if filed, and thus, no reference can be made to such return to determine New York partner allocation percentages . It is not established by the record whether Midland had a New York office, but petitioner's K-1 (Finding of Fact "12") seems to indicate so by the address referenced thereon. According to petitioner's representative, petitioner spent many days in New York conducting partnership business, on a continuous and regular basis. Likewise, the partnership agreement did not establish a New York allocation as it was missing pertinent pages. Accordingly, petitioner did not carry his burden of proof to show that his nonresident income should have been allocated to sources in New York as well as outside New York (Tax Law § 689[e]). Having insufficient records to verify petitioner's allocation of income outside New York, the Division was left with no choice and acted properly in deeming all of petitioner's nonresident income from New York sources.

E. Petitioner's Form IT-203 should have been filed with New York income allocated on the basis of New York partnership percentages, vis-a-vis the partnership return or the partnership agreement. That, however, was not done. Mr. Lenihan claims that for 18 years petitioner has

filed on a sales allocation method. He prepared the original 1999 and 2000 returns, as well as the amended returns for all three years. The 1999 and 2000 original returns clearly show they were prepared using an allocation method based on the number of days worked in New York over total days worked, and not prepared in accordance with Midland's New York partnership allocation percentages or by any method that concerns sales. By submitting the original returns on the basis of a days allocation method, petitioner in effect requested authorization for the Division to accept a calculation under an alternative method (Tax Law § 632[d]). Upon audit, the Division agreed to allow the days allocation method for the purpose of determining petitioner's nonresident income taxable to New York. Thus, petitioner is deemed to have received approval for an alternative allocation method for the years under audit based upon the number of days worked in New York/total days worked. The Division then properly requested substantiation of the method being used.

F. Before petitioner was willing to provide any substantiation, he continually referred to an agreement made between him and the Division in a prior audit, which was followed for many years thereafter. Pursuant to this agreement, the New York allocation of petitioner's nonresident income was calculated based upon sales to New York/total sales everywhere. Petitioner was unable to produce any documentation which supported that such agreement existed, either by the records of those audits maintained by his representative or by many FOIL requests. It is unclear why no documentary evidence of such an important agreement was provided. Since the agreement was so critical to the calculation of petitioner's nonresident New York income each year, it would not seem unduly difficult for either petitioner or his representative to produce some evidence in support of their assertion. What we are left with is merely the uncorroborated testimony of a representative who has provided conflicting

information throughout the hearing. Accordingly, petitioner cannot establish any due process violation where the Division could be accused of retroactively applying a different method than allowed in the past, creating a tax liability that petitioner could not have anticipated.

G. The final issue to be addressed is whether petitioner substantiated his days worked in New York compared to his days worked in all locations in order to allocate only a portion of his income to New York.

The method under which the Division has approved petitioner's allocation to New York is like that of a nonresident employee or corporate officer who performs services for his employer both within and without New York State (Tax Law § 631[c]; 20 NYCRR 132.18). They are required to establish by clear and convincing evidence the number of days they spent not working, the number of days spent in New York on business, and the number of days worked in locations other than New York (20 NYCRR 132.18), but the specific records required to do so are not delineated. Even the regulation governing New York statutory residents, 20 NYCRR 105.20, only speaks to the requirement of "adequate records." What has been submitted as substantiation in this case are diaries for the three tax years with scant and somewhat illegible notations or abbreviations, names of people, some company names, none of which have a business purpose stated, few of which have detailed locations of the meeting place, all in the same penmanship, created in two colors of red felt tip type pens. It is not clear that the entries were contemporaneously made, even where legible. Some days are left completely blank. The hearing did not shed light on petitioner's habit of work, pattern of travel, if any existed, or much in the way of details about his work for Midland, or Midland's location and operations. There were no expense reports, work summaries or any other documentation which would support

petitioner's business activities and locations. Many of the entries were made near a lunch or dinner hour, without an obvious business connection.

The other documents submitted were American Express statements for 1998 and 1999 only, showing charges to what appear to be restaurants, a few airlines and some rental car companies, which when taken together, place petitioner in locations either inside or outside New York. However, nothing establishes a business purpose. The charges to vendors are not in any way explained, thus the purpose of the charge is often unclear. Some appear as a charge to a different transaction day than petitioner's diary claimed the travel took place, without ticket stubs, airline itinerary or other substantiation. On a majority of days, there were no American Express charges or any other documentation to place petitioner in a particular location.

Mr. Lenihan met with petitioner before the hearing to clarify the diary entries. Mr. Lenihan explained that petitioner was unable to appear at the hearing due to illness. No medical evidence of his inability to attend the hearing was provided, however. In addition, no affidavit from petitioner was prepared which could have described his own medical condition and set forth much of the information that Mr. Lenihan attempted to portray by his own testimony. Thus, the issue is raised as to whether Mr. Lenihan's testimony can supplement the diaries sufficiently to provide the missing information.

In determining whether taxpayers were residents of New York by virtue of spending more than 183 days therein, the Tax Appeals Tribunal in ***Matter of Avildsen***, (May 19, 1994) held that there is no support in the statute or regulations that would lead to a conclusion that testimony alone was insufficient as a matter of law to prove such fact. But the Tribunal cautioned:

> Obviously, any taxpayer who attempts to sustain his burden of proof solely on testimonial evidence runs a very great risk that he will not prevail at the

> hearing because the Administrative Law Judge will determine that the testimony is not credible to establish the necessary facts (***id***).

The issue is narrowed to whether Mr. Lenihan's testimony, despite its characterization as hearsay, permissible in an administrative setting, was credible, and then sufficient to establish the missing facts.

Mr. Lenihan's posture throughout the audit process and the hearing was evasive and elusive. He was not forthcoming with information to support petitioner's position, be it on the alleged allocation agreement, or the handling of partnership income. He avoided the introduction of other documents from the audit files of petitioner which he claimed addressed the exact same issues. He provided little information about petitioner's business activities, locations and associations. He provided no substantiation for petitioner's alleged medical incapacity to appear at the hearing, or any affidavit from petitioner to supplement missing facts. Not only did he improperly prepare petitioner's nonresident returns for the years in issue, whether it was on the basis of sales or days, but his characterization of the method of allocation of petitioner's nonresident income for at least 1999 and 2000 was inaccurate and misleading. He claimed the returns were filed on the sales method, when he had filed them on the days method. In addition, the record contains three conflicting allocation schedules of days worked in and out of New York for the years in issue (***see*** Findings of Fact "3," "14" and "15") for all of which Mr. Lenihan was involved in the preparation. I am unable to find Mr. Lenihan's testimony credible and reliable in this matter, and it was clearly lacking in sufficient details to establish the missing factual content. If petitioner was a traveling sales representative for Midland who spent a significant number of days outside New York State on business, it was incumbent upon him to contemporaneously maintain records to substantiate the same. Petitioner was allegedly in this type of business environment for many years and was put on notice not only by law, but in prior

audits, as to what information would be required of him. If his records were lacking and he was in fact too ill to appear at the hearing to now establish such facts by his own testimony, he was still under an obligation to substantiate these facts to build his case. Petitioner did not meet even a small portion of this burden.

Accordingly, the Division properly determined that petitioner had not substantiated his business days in New York and elsewhere.

H. The wages which were allocated to New York by the Division were allegedly earned by petitioner from a different company, after he left Midland in September 2000. Petitioner claims this to be only Connecticut income. However, no documentation of any kind, including a W-2, was produced to indicate the details of that employment, when petitioner started this job, where the employer was located or where petitioner performed services. Accordingly, the Division also properly deemed the wage income in 2000 all New York source income.

I. The petition of John and Caroline Gould is hereby denied and the Division's Notice of Deficiency dated October 28, 2002, is sustained.

DATED: Troy, New York
March 16, 2006

/s/ Catherine M. Bennett
ADMINISTRATIVE LAW JUDGE