

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition :  
of :  
Donald A. Leventhal :  
and Sheila S. Leventhal :  
: AFFIDAVIT OF MAILING  
for Redetermination of a Deficiency or a Revision :  
of a Determination or a Refund of Gift Tax under :  
Article 26A of the Tax Law for the Year 1975.

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State of New York  
County of Albany

Jay Vredenburg, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 20th day of November, 1981, he served the within notice of Decision by certified mail upon Donald A. Leventhal and Sheila S. Leventhal, the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Donald A. Leventhal  
and Sheila S. Leventhal  
583 Ocean Terrace  
Staten Is., NY 10301

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this  
20th day of November, 1981.

*Carrie A. Hays*

*J. Vredenburg*

STATE OF NEW YORK  
STATE TAX COMMISSION

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In the Matter of the Petition :  
of :  
Donald A. Leventhal :  
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for Redetermination of a Deficiency or a Revision  
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Article 26A of the Tax Law for the Year 1975.

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State of New York  
County of Albany

Jay Vredenburg, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 20th day of November, 1981, he served the within notice of Decision by certified mail upon Richard D. Kuhn the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Richard D. Kuhn  
Holzka, Donahue, Kuhn & Howard  
358 St. Marks Pl.  
Staten Is., NY 10301

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this  
20th day of November, 1981.

*Annice A. Haylund*

*J. Vredenburg*

STATE OF NEW YORK  
STATE TAX COMMISSION  
ALBANY, NEW YORK 12227

November 20, 1981

Donald A. Leventhal  
and Sheila S. Leventhal  
583 Ocean Terrace  
Staten Is., NY 10301

Dear Mr. & Mrs. Leventhal:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1007b of the Tax Law, any proceeding in court to review an adverse decision by the State Tax Commission can only be instituted under Article 78 of the Civil Practice Laws and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance  
Deputy Commissioner and Counsel  
Albany, New York 12227  
Phone # (518) 457-6240

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative  
Richard D. Kuhn  
Holzka, Donahue, Kuhn & Howard  
358 St. Marks Pl.  
Staten Is., NY 10301  
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petitions  
of  
DONALD A. & SHEILA S. LEVENTHAL  
for Redetermination of a Deficiency or for  
Refund of Gift Tax under Article 26A of the  
Tax Law for the Year 1975.

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DECISION

Petitioners, Donald A. and Sheila S. Leventhal, 583 Ocean Terrace, Staten Island, New York 10301, filed petitions for redetermination of a deficiency or for refund of gift tax under Article 26A of the Tax Law for the year 1975 (File Nos. 22902 and 22903).

A formal hearing was held before Robert A. Couze, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York on March 13, 1981 at 10:40 A.M. Petitioners appeared by Holzka, Donahue, Kuhn & Howard, Esqs. (Richard D. Kuhn and Steven P. Howard, Esqs., of counsel). The Audit Division appeared by Ralph J. Vecchio, Esq., (Irwin Levy, Esq., of counsel).

ISSUE

Whether petitioners' method of valuing their gift of the income interest in a trust they created was proper for gift tax purposes.

FINDINGS OF FACT

1. On May 8, 1978 the Audit Division issued against each petitioner, Donald A. and Sheila S. Leventhal, a timely Notice of Deficiency.
2. The statements of audit changes on which the notices of deficiency are based, read in part as follows:

"The value of the income interest gifted under the trust agreement has been revised to a total of \$111,675.00 (\$55,837.50 applicable to each spouse), to reflect the present value of the income stream for a period of 10 Years 9 months as per the trust instrument. In view of the fact that the property is leased, the present worth of the income has been valued based upon the lease.

The annual deduction of \$3,000.00 each for three (3) donees has been disallowed under Reg. 25 Section 2503-4 of the Internal Revenue Code as the income may be accumulated and does not necessarily go to the beneficiaries when they reach age 21. This constitutes a gift of future interest.

Taxable Gifts as Reported	\$10,300.00	Total Tax Due	881.34
Tax Due as Reported	162.00	Previous Payment	162.00
Adjusted Taxable Gifts	55,837.50	Add'l Tax Due	<u>719.34</u>
Adjusted Tax Due	881.34		
		Total Interest Due	86.12
		Previous Payment	1.70
		Add'l Int. Due	<u>84.42</u>
		Total Penalty Due	88.13
		Previous Payment	16.20
		Add'l Penalty Due	<u>71.93</u>
		Balance Due	\$875.69"

3. On April 1, 1975, petitioners, Donald A. Leventhal, and his wife, Sheila S. Leventhal, created a Trust naming Donald A. Leventhal as Trustee. The Trust was to last for a period of ten (10) years six (6) months and provided for income to be distributed or accumulated for the benefit of petitioners' three (3) sons. Petitioners transferred and delivered certain real property to the Trust, and the trust agreement was recorded in the Richmond County Clerk's Office. The property, located at 2877 Hylan Boulevard, Staten Island, New York, was at that time occupied by Donald A. Leventhal, D.D.S., P.C., a professional corporation engaged in the practice of dentistry.

4. Thereafter, the Trust, as landlord, entered into a net lease with the professional corporation, as tenant. This lease provided, among other things, for the payment to the Trust of \$14,400.00 in rental per annum. The lease was

for a two (2) year term, and the tenant was to bear all expenses in connection with the property so that the lease was net to the landlord-Trust.

5. The \$14,400.00 annual rental figure for the two (2) year lease term was based upon the fair market value of the property. A few years prior to 1975, appraisals of the property determined the value to then be approximately \$55,000.00 to \$60,000.00. Applying a 10% increase in general real estate values per year since the time of those appraisals, petitioners concluded that in 1975, the property had a fair market value of approximately \$90,000.00. The annual rental figure in the lease was intended to give the Trust a 15% - 16% percent yearly return on an investment that was worth about \$90,000.00, a figure which petitioners thought was reasonable under all the circumstances.

6. The appraisals upon which petitioners based their computation were put in evidence at the hearing. Also put in evidence was a more recent appraisal by one Joseph E. Walsh, a real estate appraiser, showing that the fair market value of the real property in question was approximately \$100,000.00 at the time the gift was made in 1975.

7. A few months after the Trust was created, petitioner Donald A. Leventhal resigned as Trustee and petitioner Sheila S. Leventhal renounced her right to succeed him as Trustee. Thereafter, one Ronald Leventhal became Trustee.

8. All leases after the expiration of the first two (2) year lease were negotiated between Ronald Leventhal, as Trustee on behalf of the landlord-Trust, and Donald A. Leventhal, acting on behalf of the professional corporation, as tenant.

9. For gift tax purposes, petitioners considered that a gift was made of an income interest for the duration of the Trust. The value of the gift was

determined on the basis of the standard 6% valuation tables as published by the Internal Revenue Service, which tables (Treasury Valuation Table B, Column 3 [Term Certain]) showed that the gift of an income interest for a term certain had a value of about 44% of the total value of the property. Since the property had a fair market value at the time of the gift of approximately \$90,000.00, taxpayer reported 44% of that amount, or \$39,600.00, as the value of the gift in 1975.

10. The Audit Division argued that petitioners' valuation of the gift was erroneously computed. The Audit Division redetermined the value of the gift by the "lease-projected income" method, whereby the value of the gift was computed by multiplying the dollar amount of the annual rental of the first year of the lease times the Trust's period of duration (approximately ten [10] years). Thus the \$14,400.00 first year rental income from the lease times ten (10) years results in a gift value of \$144,400.00. This, the Audit Division argued, was what the Trust was likely to receive in rental income over the term of the Trust.

11. Petitioners, on the other hand, argue that they properly used the "term certain" method to value the gift since there was no guarantee that the Trust would receive the \$14,400.00 annual rental in each of the ten (10) years of the Trust. They argue that the leases were only for two (2) year terms, were negotiable at the time of renewal, and that the amount of rental income and certainty of its payment depended upon such factors as the continued success of the professional corporation's practice of dentistry and the personal health of petitioner Donald A. Leventhal.

12. Petitioners also considered their gift to have been that of a present interest, and accordingly each petitioner claimed an exclusion of \$3,000.00 for

each of the three (3) donees. None of the three (3) donees had attained the age of twenty one (21) years as of the date of the gift. The Audit Division disallowed the above exclusions on the basis that petitioners' gift was of a future interest rather than a present interest (Finding of Fact "2", supra). At the hearing, petitioners did not contest that portion of the deficiency relating to the disallowance of the claimed exclusions.

13. The Audit Division failed to adopt any formula to compute the present "dollar value" of the future interest at the time of the gift.

14. In 1977, petitioner Donald A. Leventhal conveyed his reversionary interest in the property to petitioner Shiela A. Leventhal. The value of this gift, for gift tax purposes, was also determined by reference to the 6% standard valuation tables published by the Internal Revenue Service. The State, however, has not contested the valuation of this reversionary interest nor the method used to determine that value.

15. The record is silent as to any position the Internal Revenue Service may or may not have taken with regard to taxing the gift.

#### CONCLUSIONS OF LAW

A. That Revenue Ruling 59-60, section 2.02, cites to Federal Estate and Gift Tax Regulations which "...define fair market value, in effect, as the price at which the property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell...".

B. That the price a willing buyer would pay for the future interest of petitioners' gift would not be the total value of the future gift but instead the future gift's total value less its reasonable discount rate.

C. That petitioners, by the use of independent appraisals, properly established the fair market value of the property they placed in trust.

D. That Treasury Regulations sections 25.2511-1(e), 25.2512-5(a)(1) and 25.2512-9(a)(1)(i) refer to the 6 percent valuation tables published by the Internal Revenue Service as the proper means of determining the gift tax value of an income interest in property. (See Revenue Ruling 58-242, 1958-1 CB 251). This method of valuation must be used unless it is shown that the result would be unrealistic and unreasonable, and that a more reasonable and realistic means of determining value is available. Weller v. Commissioner, 38 T.C. 790, (1962), Vernon v. Commissioner, 66 T.C. 484 (1976). See also Revenue Ruling 77-195, 1977-1 CB 295.

E. That where a donor transfers property in trust or otherwise and retains an interest in the property, the value of the gift for gift tax purposes is the value of the property transferred minus the ascertainable value of the donor's retained interest in the property, actuarially computed. See Authority cited in Conclusion of Law "D" (supra). See also Research Institute of America, Federal Tax Coordinator 2d, Volume 21, page 42,316, paragraph P-6651.

F. That petitioners' method of valuing their gift of the income interest flowing from the property placed in trust resulted in the correct "dollar valuation" of that gift for gift tax purposes.

G. That petitioners' gift did not constitute the gift of a present interest within the meaning and intent of subsection (b) or (c) of section 2503 of the Internal Revenue Code and Regulations thereunder, and thus the Audit Division properly disallowed the \$3,000.00 exclusions referred to in Findings of Fact "2" and "12".

H. That the Audit Division is directed to recompute the notices of deficiency against petitioners to reflect the disallowed exclusions referred to in Conclusion of Law "G", and that except as provided in Conclusion of Law "G", the petitions of Donald A. and Sheila S. Leventhal are granted and the notices of deficiency are cancelled.

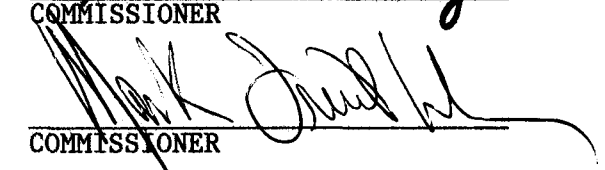
DATED: Albany, New York

NOV 20 1981

STATE TAX COMMISSION

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER