

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Albert Lederman :
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 Period Ending :
12/31/76 & 3/31/77. :
_____ :

AFFIDAVIT OF MAILING

State of New York
County of Albany

David Parchuck, 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 27th day of May, 1983, he served the within notice of Decision by certified mail upon Albert Lederman, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Albert Lederman
9 Willow Brook Rd.
White Plains, NY 10605

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
27th day of May, 1983.

David Parchuck

James A. DeGale

AUTHORIZED TO ADMINISTER
OATHS PURSUANT TO TAX LAW
SECTION 174

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Albert Lederman :
AFFIDAVIT OF MAILING
for Redetermination of a Deficiency or a Revision :
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Article 26A of the Tax Law for the Period Ending :
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State of New York
County of Albany

David Parchuck, 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 27th day of May, 1983, he served the within notice of Decision by certified mail upon H. B. Carroll the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

H. B. Carroll
Cummings & Carroll
175 Great Neck Rd.
Great Neck, NY 11021

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
27th day of May, 1983.

David Parchuck

James A. Heyland

AUTHORIZED TO ADMINISTER
OATHS PURSUANT TO TAX LAW
SECTION 174

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

May 27, 1983

Albert Lederman
9 Willow Brook Rd.
White Plains, NY 10605

Dear Mr. Lederman:

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) 690 & 1007 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 Law 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
Law Bureau - Litigation Unit
Building #9 State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
H. B. Carroll
Cummings & Carroll
175 Great Neck Rd.
Great Neck, NY 11021
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
	:	
of	:	
ALBERT LEDERMAN	:	DECISION
	:	
for Redetermination of a Deficiency or for	:	
Refund of Gift Tax under Article 26-A of the	:	
Tax Law for the Quarters Ending December 31,	:	
1976 and March 31, 1977.	:	

Petitioner, Albert Lederman, 9 Willow Brook Road, White Plains, New York 10605, filed a petition for redetermination of a deficiency or for refund of gift tax under Article 26-A of the Tax Law for the quarters ending December 31, 1976 and March 31, 1977 (File No. 23117).

On August 25, 1982, petitioner, by his representative, Cummings & Carroll, P.C. (H. B. Carroll, CPA), waived a formal hearing and requested the Tax Commission to render its decision on the file as presently constituted.

ISSUE

Whether the Audit Division properly valued stock in a closely-held corporation, the subject of the gifts at issue, by using a weighted average valuation method applied to net earnings and a capitalization rate of 10 percent.

FINDINGS OF FACT

1. On or about January 17, 1977, petitioner, Albert Lederman, filed a New York State Resident Quarterly Gift Tax Return for the quarter ending December 31, 1976, reporting New York taxable gifts in the amount of \$30,592.00 and calculating and remitting gift tax of \$458.88. Petitioner's United States Quarterly Gift Tax Return for the same period contained a description of one of the gifts herein at issue: to his wife, Jewel Lederman, 9 shares of common stock of

Jakwel Sales Corp. ("Jakwel"), located at 150 River Street, Hastings-on-Hudson, New York.

On or about May 5, 1977, petitioner filed a New York State Resident Quarterly Gift Tax Return for the quarter ending March 31, 1977, reporting New York taxable gifts in the amount of \$38,057.00 and calculating and remitting gift tax of \$710.72. Petitioner's federal gift tax return for the same quarter contained a description of the second gift at issue: to Jewel Lederman, 11 shares of common stock of Jakwel.

For purposes of the tax, petitioner valued the common stock of Jakwel by using the book value and applying thereto an additional 20 percent for goodwill.

2. On June 19, 1978, the Audit Division issued to Mr. Lederman a Notice of Deficiency, asserting additional gift tax due for the quarters ending December 31, 1976 and March 31, 1977 in the respective amounts of \$256.73 and \$599.05, plus interest thereon. The Statement of Audit Changes, issued to petitioner on October 11, 1977, explained that in computing the asserted deficiencies, the Audit Division had "estimated the value of the stock of the corporation by using a weighted average valuation method applied to net earnings and a capitalization rate of 10%." The Audit Division's computation of the adjusted taxable gifts is shown below.

(a) Computation of per share value

<u>YEAR</u>	<u>NET EARNINGS</u>	<u>FACTOR</u>	<u>TOTAL</u>
1976	\$272,559	5	\$1,362,795
1975	253,014	4	1,012,056
1974	184,234	3	552,702
1973	165,138	2	330,276
1972	122,679	1	122,679
	<u>\$997,624</u>		<u>\$3,380,508</u>

$\$3,380,508/15 = \$225,367.20$ weighted average net earnings
 $\$225,367.20 \times$ capitalization factor of 10 = $\$2,253,672$
value of 200 shares

value per share = $\$11,268.36$

(b) Gift during quarter ending December 31, 1976

$\$11,268.36 \times 9$ shares	=	$\$101,415.24$	total gift
		$(50,707.62)$	marital deduction
		$(3,000.00)$	annual exclusion
		$\$ 47,707.62$	adjusted taxable gift
		$\$ 715.61$	tax due
		(458.88)	tax paid
		$\$ 256.73$	balance

(c) Gift during quarter ending March 31, 1977

$\$11,268.36 \times 11$ shares	=	$\$123,951.96$	total gift
		$(61,975.98)$	marital deduction
		$(3,000.00)$	annual exclusion
		$\$ 58,975.98$	adjusted taxable gift
		$\$ 1,309.77$	tax due
		(710.72)	tax paid
		$\$ 599.05$	balance

3. Petitioner was the president and majority shareholder of Jakwel, which was engaged in the business of rack jobbing. Jakwel purchased items, such as cosmetics, hair care products, party goods and stationery, which can be readily displayed in and sold from racks. Jakwel resold the items to discount drug stores and other discount general merchandise stores. Petitioner considered Jakwel primarily a service corporation, which eliminated any need for warehousing on the part of its customers.

4. At the time in question, Jakwel had 16 customers, 6 of which accounted for approximately 84 percent of all the company's sales. Jakwel did not employ any sales representatives. All of its customers had been obtained and were served by petitioner.

5. Jakwel never paid any dividends.

6. No attempts were made to sell Jakwel stock to the public before or after petitioner's valuation of the stock for gift tax purposes.

7. On March 1, 1982, substantially all the assets of Jakwel, along with the corporate name and a covenant not to compete, were sold for \$159,646.00. Jakwel's inventory was sold, the price determined in accordance with a formula set forth in the contract of sale. Also constituting part of the agreement between Jakwel and the purchaser was an employment contract, by the terms of which Mr. Lederman was to be employed full-time by the purchaser at a base compensation of \$75,000.00 per annum.

On May 4, 1982, Mr. Carroll (petitioner's representative) submitted the contract of sale to the Audit Division and stated in his letter accompanying the contract:

"The sale of substantially all the assets of the Corporation on March 1, 1982 was made at book value plus a small amount, namely \$10,000 for the corporate name and a covenant not to compete (Article I, paragraph 6).

"It is our contention that the original valuation on the gift tax returns was proper in light of the fact that the Corporation was sold for close to book value..."

8. The Internal Revenue Service examined petitioner's federal gift tax returns for the quarters ending December 31, 1976 and March 31, 1977 and made no adjustments thereto.

CONCLUSIONS OF LAW

A. That section 1009 of the Tax Law provides that the gift tax provisions of the Internal Revenue Code of 1954 shall apply to the determination of New York gift tax to the extent specified in Article 26-A. Section 2512(a) of the Code provides that if a gift is made in property, the value thereof on the date of the gift shall be considered the amount of the gift.

B. That in valuing stock in the absence of sale and bid prices therefor, federal gift tax regulations provide that the corporation's net worth, prospective earning power, dividend-paying capacity and other relevant factors are to be taken into consideration. Treas. Reg. Sec. 25.2512-2(f). In general, primary consideration is accorded to earnings, when valuing stock of companies which sell products or services to the public; conversely, in the case of an investment or holding company, greatest weight may be accorded to the assets underlying the stock to be valued. Rev. Rul. 59-60, 1959-1 C.B. 237, modified by Rev. Rul. 65-193, 1965-2 C.B. 370; Matter of Leonard and Rose Frank, State Tax Comm., April 9, 1982; Matter of Clifford J. Lamb, State Tax Comm., October 3, 1980.

C. That petitioner's method of valuation is more appropriately applied to investment and holding companies and cannot be adopted herein. Heavy investment in business assets was not needed to generate additional sales by Jakwel, a service business.

The stock of Jakwel, a corporation engaged in the sale of products and services to discount stores, was properly valued according to its average earnings over the 5-year period 1972 through 1976. (E.g., Korslin v. United States, 73-1 U.S.T.C. (CCH) ¶12,907 (E.D. Wis.) wherein, for estate tax purposes, the court valued stock in a close corporation, which manufactured refrigeration and beer dispensing equipment principally for the brewing industry, by applying a multiple of 9 to the average per share earnings over the 5-year period preceding decedent's death.)

As a result of the gifts at issue, petitioner's wife received a minority interest in Jakwel (20 shares of 200 shares outstanding); a 30 percent

reduction to the per share value is accordingly permissible, to take account of the limited marketability of the shares.

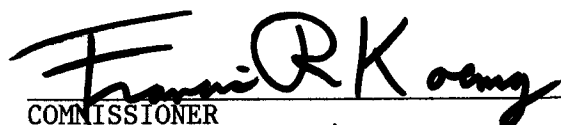
D. That the petition of Albert Lederman is granted to the extent indicated in Conclusion of Law "C"; that the Notice of Deficiency issued on June 19, 1978 is to be modified accordingly; and that except as so modified, the deficiency is in all other respects sustained.



DATED: Albany, New York

STATE TAX COMMISSION

MAY 27 1983


PRESIDENT


COMMISSIONER

 
COMMISSIONER