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Income Tax Determinations, 1968
A-2

BUREAU OF LAW

MEMORANDUM *Napoli, Fanny*
Nate
Thomas

TO: State Tax Commission

FROM: Vincent P. Molineaux, Hearing Officer

SUBJECT: NAPOLI, NATE & FANNY
NAPOLI, THOMAS

Applications for Revision or Refund
of Personal Income Taxes under Article 16
of the Tax Law for the Year 1959

The issue raised herein is whether a loss incurred on the sale of real estate owned by a partnership and claimed as an ordinary loss, was (a) a normal loss or (b) a capital loss which could not be offset against the normal income of the partnership.

1608 Ocean Parkway Towers Company, a partnership consisting of the applicants and two other partners were the owners of a 49 apartment house which they rented directly to the occupants. They had two employees. In 1959 the partnership sold the premises, incurring a loss of \$77,806.31. This loss was distributed among the four partners and each of the partners claimed the amount of \$19,451.78, one-quarter of the total loss, as a normal loss deductible from normal income.

The losses were disallowed by the Department as normal losses, on the ground that the partnership was not engaged in a trade or business but were merely engaged in renting for investment purposes and that the real estate was capital assets of the partnership not used in a trade or business. Accordingly, only capital loss treatment was allowed.

The taxpayers contend that the Federal government allowed the losses as ordinary losses and that the assets were not capital assets either pursuant to the Internal Revenue Code or to Section 350 of Article 16 of the Tax Law in effect during the year in issue.

No assessment against the partnership for unincorporated business taxes was made.

Section 386 of the Tax Law exempts from the unincorporated business tax the activities of the holding, leasing or management of real property by an owner, lessee or fiduciary. Since it is

evident here that the partnership was engaged solely in the holding, leasing and management of real property it is exempt from the unincorporated business tax. The question therefore is whether an entity exempt from unincorporated business tax can be deemed to be carrying on a trade or business with respect to the issue of capital treatment so that the loss on the sale of its assets could be deemed an ordinary loss and not a capital loss.

The Federal tax treatment allowing the taxpayer an ordinary loss did not involve consideration of the question whether or not the partnership was engaged in a trade or business. The reason for this is that the ordinary loss was allowed under Section 1231 of the Internal Revenue Code which permits gains on the sale of business property held for more than six months to be considered capital gains, and losses on business property held for more than six months to be considered as ordinary losses. Thus, in conformity years (1960 and subsequent) the question raised herein cannot ordinarily arise because of conformity with Federal treatment. The year in issue, however, is a pre-conformity year. It is to be noted, further, that the question of capital gains or ordinary income treatment will continue to arise when the asset is held for not more than six months.

In the Case of Appleby v. Bates, 278 App. Div. 12, 103 N Y S 2d 317 the Appellate Division of the New York State Supreme Court held on March 17, 1951 that the ownership of real estate, the renting and management of the same, by an estate for the purpose of paying off the debts of a decedent who had owned the real estate was an investment not a trade or business and that the collection of rents and making of necessary repairs did not convert the operation into a trade or business. The Court there held "We are not bound where our tax policy may differ from the way the United States may have treated the property for tax purposes."

More than ten years later the Appellate Division, Third Department in the Case of George W. Warnecke v. State Tax Commission, 15 A D 2d 320 modified the position taken in Appleby v. Bates. There the Court held that the operation of an apartment hotel and lobby restaurant was the holding, leasing and management of real property exempting such transactions from the unincorporated business tax but that the activities in operating the hotel and restaurant were far more than the mere "general management of collecting rents and making repairs" and that the gain realized on the sale of the property was not a capital gain but ordinary income. The Court there held that the "Commission's denial of capital gains treatment is consistent also with decisions under

similar Federal statutes." The Court cited Gilford v. Commissioner of Internal Revenue, 201 F. 2d 735 and the cases there cited.

In the Gilford case, supra, decided in 1953, parcels of property inherited under will and placed in the hands of real estate agents which managed the properties were held to be property used in a trade or business, and not subject to capital gains treatment.

Federal treatment has generally held that the renting of properties requiring considerable attention for advertising, tenants, repairing, etc. was a trade or business resulting in ordinary income to the taxpayer. Hazard, 7 T.C. 72; Fackler, 43-1 USTC 9270, 133 F. 2d 509. The chief exception was that of Isabel H. Grier v. United States, 55-1 USTC para. 9184, 218 F. 2d 503. In that case Grier acquired a one family home by inheritance, collected the rent and made the necessary repairs. The Court held that since there was no activity to rent and re-rent and no employee regularly engaged for maintenance and repair, the property was held for investment purposes.

The cases of Appleby v. Bates and Grier v. the United States, can be distinguished in that the Court found as facts mere passive management and a minimum amount of labor necessary to keep the place in repairs. The facts in the instant case before us are different. Here the partnership was in the active renting of a large apartment house. The partnership hired employees and engaged in the rental of the apartments as a business venture. I am therefore of the opinion that the assets were used in a trade or business of the taxpayer and that the loss on the sale of real property was an ordinary loss. The assessments should accordingly be cancelled.

/s/

VINCENT P. MOLINEAUX

Hearing Officer

June 3, 1968
VPM:nn

6-20-68

STATE OF NEW YORK
STATE TAX COMMISSION

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IN THE MATTER OF THE APPLICATION :
OF :
NAPOLI, MATE & FANNY :
FOR REVISION OR REFUND OF PERSONAL :
INCOME TAXES UNDER ARTICLE 18 OF THE :
TAX LAW FOR THE YEAR 1959 :
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The taxpayers herein, having filed an application for revision or refund of personal income taxes under Article 18 of the Tax Law for the calendar year 1959, and a hearing having been held in connection therewith at the office of the State Tax Commission, 80 Centre Street, New York, New York on the 26th day of May, 1965 before Vincent P. Molineaux, Hearing Officer of the Department of Taxation and Finance, and the record having been duly examined and considered,

The State Tax Commission hereby finds:

(1) That the taxpayer, Mate Napoli was a 25% partner in a partnership which called itself 1688 Ocean Parkway Towers Company.

(2) That the partnership was the owner of a 40 apartment house which they rented directly to the occupants and that the partnership had two employees and incurred other advertising, administrative and operating expenses.

(3) That in 1959 the partnership sold the premises, incurring a loss of \$77,808.31 which loss was distributed among the four partners and the partners, Mate and Fanny Napoli, reported a normal loss of \$19,451.78.

(4) That the deduction was disallowed and Assessment No. B 874531 in the amount of \$1,258.76 was issued December 1, 1968 on the ground that the loss was a capital loss and could not be set off against normal gains.

Based upon the foregoing findings and all of the evidence presented herein, the State Tax Commission hereby

DETERMINES:

(A) That the partnership was carrying on a trade or business of operating and renting a large apartment house and that the loss on the sale of the real property was an ordinary loss.

(B) That, accordingly, the application for revision of Assessment No. B 878461 for the year 1959 is hereby granted.

(C) That Assessment No. B 878461 is cancelled in full.

DATED: Albany, New York this 21st day of August, 1968.

STATE TAX COMMISSION

/s/

JOSEPH H. MURPHY
President

/s/

A. BRUCE MANLEY
Commissioner

/s/

SAMUEL E. LEPLER
Commissioner

STATE OF NEW YORK

STATE TAX COMMISSION

IN THE MATTER OF THE APPLICATION :
OF :
THOMAS NAPOLI :
FOR REVISION OR REFUND OF PERSONAL :
INCOME TAXES UNDER ARTICLE 16 OF THE :
TAX LAW FOR THE YEAR 1959 :

The taxpayer herein, having filed an application for revision or refund of personal income taxes under Article 16 of the Tax Law for the calendar year 1959, and a hearing having been held in connection therewith at the office of the State Tax Commission, 80 Centre Street, New York, New York on the 28th day of May, 1966 before Vincent P. Molineaux, Hearing Officer of the Department of Taxation and Finance, and the record having been duly examined and considered,

The State Tax Commission hereby finds:

(1) That the taxpayer, Thomas Napoli was a 25% partner in a partnership which called itself 1508 Ocean Parkway Towers Company.

(2) That the partnership was the owner of a 40 apartment house which they rented directly to the occupants and that the partnership had two employees and incurred other advertising, administrative and operating expenses.

(3) That in 1959 the partnership sold the premises, incurring a loss of \$77,806.31 which loss was distributed among the four partners and the partner, Thomas Napoli, reported a normal loss of \$19,451.78.

(4) That the deduction was disallowed and Assessment No. B 824531 in the amount of \$1,258.75 was issued December 1, 1960 on the ground that the loss was a capital loss and could not be set off against normal gains.

Based upon the foregoing findings and all of the evidence presented herein, the State Tax Commission hereby

DETERMINES:

(A) That the partnership was carrying on a trade or business of operating and renting a large apartment house and that the loss on the sale of the real property was an ordinary loss.

(B) That, accordingly, the application for revision of Assessment No. B 824531 for the year 1959 is hereby granted.

(C) That Assessment No. B 824531 is cancelled in full.

DATED: Albany, New York this 21st day of August, 1968.

STATE TAX COMMISSION

/s/

JOSEPH H. MURPHY
President

/s/

A. BRUCE MANLEY
Commissioner

Commissioner