STATE OF NEW YORK
STATE TAX COMMISSION

In the Matter of the Petition :
of
John W. & Dorothy B. Galbreath :

AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or a Revision :
of a Determination or a Refund of
Personal Income & UBT :
under Article 22 & 23 of the Tax Law
for the Years 1965 - 1967. :

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 17th day of October, 1980, he served the within notice of Decision by certified mail upon John W. & Dorothy B. Galbreath, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

John W. & Dorothy B. Galbreath
100 East Broad St.
Columbus, Ohio 43215

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
17th day of October, 1980.

Deborah A Bank

STATE OF NEW YORK
STATE TAX COMMISSION

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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 17th day of October, 1980, he served the within notice of Decision by certified mail upon Stephen R. Field the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Mr. Stephen R. Field
Burns, Jackson, Miller, Summit & Jacoby
445 Park Ave.
New York, NY 10022

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
17th day of October, 1980.

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

October 17, 1980

John W. & Dorothy B. Galbreath
100 East Broad St.
Columbus, Ohio 43215

Mr. & Mrs. Galbreath:

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 & 722 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
Stephen R. Field
Burns, Jackson, Miller, Summit & Jacoby
445 Park Ave.
New York, NY 10022
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition of JOHN W. GALBREATH and DOROTHY B. GALBREATH for Redetermination of a Deficiency or for Refund of Personal Income and Unincorporated Business Taxes under Articles 22 and 23 of the Tax Law for the Years 1965, 1966 and 1967.	DECISION

Petitioners, John W. Galbreath and Dorothy B. Galbreath, 100 East Broad Street, Columbus, Ohio 43215, filed a petition for redetermination of a deficiency or for refund of personal income and unincorporated business taxes under Articles 22 and 23 of the Tax Law for the years 1965, 1966 and 1967 (File No. 14390).

A formal hearing was held before Edward L. Johnson, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on July 14, 1978 at 1:15 P.M. Petitioners appeared by Burns, Jackson, Miller, Summit & Jacoby, Esqs. (Stephen R. Field and Ira B. Stechel, Esqs., of counsel). The Audit Division appeared by Peter Crotty, Esq. (Bruce M. Zalaman, Esq., of counsel).

ISSUES

I. Whether the racing of horses, the training and breeding of horses and farming constituted a single business.

II. Whether the direct accounting method used by petitioner John W. Galbreath properly reflected the net business income/loss from the racing of horses.

FINDINGS OF FACT

1. Petitioners filed joint New York State income tax nonresident returns

for the years 1965, 1966 and 1967, on which they indicated that their home address was 100 East Broad Street, Columbus, Ohio.

2. A "Consent Fixing Period of Limitation Upon Assessment of Personal Income and Unincorporated Business Taxes" was properly executed for the years 1965, 1966 and 1967 until April 15, 1974.

3. On October 29, 1973, the Audit Division issued a Notice of Deficiency imposing additional income tax liabilities for the tax years 1965, 1966 and 1967 as follows:

Years	Tax	Interest	Total
1965	$ 3,479.72	$1,573.88	$ 5,053.60
1966	6,019.58	2,361.48	8,381.06
1967	3,103.41	1,031.26	4,134.67
Total	$12,602.71	$4,966.62	$17,569.33

4. During the three years in issue, petitioners derived gross income from various sources. One source was purse income from the racing of horses owned by petitioners in competitions in different states, including New York. Another source of income was stud service income from the breeding of horses at petitioners' farm located outside of Lexington, Kentucky. No breeding operations occurred within New York. A third source of income was the proceeds derived from the sale of horses some of which sales took place in New York. A fourth source of income was the proceeds derived from the sale of undivided interests in certain horses, none of which sales took place in New York. In addition, petitioners received income from the sale of cattle and produce raised and grown on their Ohio farm.

5. The horses used for breeding in any given year would neither enter New York nor otherwise have any connection with New York, nor were any of them sold in New York during the years at issue. Instead, they were maintained at petitioners' farm outside of Lexington, Kentucky. The Lexington farm contained

a permanent staff and facilities for the purpose of breeding thoroughbred horses by bloodline.

6. The Columbus farm was used to raise corn, soybeans, wheat and hay, to fatten beef cattle and to train promising newborn horses for racing.

7. The Columbus farm was not used for breeding operations. In the usual course of petitioners' breeding business, petitioners' mares were transferred from the Columbus farm to the Lexington farm for breeding and foaling, and then both the mares and the foals were returned to Columbus. There the foals received preliminary track training, and if trackworthy, were passed on to a trainer who would further develop them for racing.

8. Petitioners' racehorses raced in Florida during the winter and were brought north as the year progressed, racing in Maryland, Kentucky, New York, New Jersey and Massachusetts. When the racing year ended in late November or early December, the racehorses either continued racing for another year, in which case they were shipped to Florida, or retired to breeding, in which case they were sent to the Lexington farm.

9. None of petitioners' horses were located in New York on December 31st of any year in issue. Likewise, at no time did petitioners maintain an office in New York with respect to their horse-related operations.

10. During the years in question, petitioners leased from owners in Europe horses which were used in petitioners' breeding operations. These leased horses never entered New York. Also, petitioners purchased some horses exclusively for breeding purposes. Similarly, petitioners owned brood mares with good bloodlines which never raced, as well as injured or otherwise physically defective mares which never raced, but were used strictly for breeding; the brood mares or injured or physically defective mares never entered New York.

11. Petitioners maintained separate, complete and accurate financial books and records for their breeding operations and for their racing operations, and recorded income and expenses as they related to each separate activity. This in turn reflected the separate identity of the horses used in the two different operations, as well as the separate facilities, operating personnel, licensing requirements and professional society memberships maintained by petitioners for each of their distinct racing and breeding operations.

12. Petitioners, for the years in issue, included on their New York State income tax nonresident returns:

(i) Salary earned from New York sources;*

(ii) Income (both ordinary and long-term capital gain) derived from sales, in New York, of racehorses;

(iii) Board incomes earned in New York; ** and

(iv) Purse income won in racing competitions in New York.

13. Petitioners, to determine the racing expenses allocable to the income described in Finding of Fact "12 (ii)", "(iii)" and "(iv)", above, apportioned the total racing expenses incurred by them in such activities for the year by a percentage representing the number of racing horse days within New York over the total racing horse days in a calendar year.***

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* During the years in question, Mr. Galbreath was an employee of Galbreath Ruffin Corporation, which managed and owned real estate in New York City and elsewhere, and from which he received an annual salary of $90,000, $90,000, and $140,000 in 1965, 1966 and 1967, respectively.

** Board income represents fees derived from persons owning racehorses who lack operating personnel to properly maintain their horses while at racetracks and therefore boarded them with the petitioners' racehorses and track personnel at times such racehorses and track personnel were in New York.

*** Horse days represent the actual number of days spent by a horse at a given track. For example, if a horse is boarded at Belmont for nine days and raced on two different days, nine horse days have been spent at Belmont (rather than two), since the petitioners have incurred the cost of upkeep for that horse at Belmont for nine days (rather than two).

14. Petitioners did not include as income subject to New York income tax any income derived from the sale of racehorses outside of New York, nor of undivided interests therein, nor any board or purse income realized outside of New York. Furthermore, since petitioners consistently regarded and treated their breeding operations as a separate entity from their racing operations, they did not report any breeding income to New York nor did they allocate any breeding expenses to New York. Likewise, petitioners also regarded their farming operations as a separate entity from their racing operations, and did not report any income from the sale of farm produce (such as hay, wheat, corn, etc.) or cattle to New York nor did they allocate any related farming expenses to New York.

15. The Audit Division rejected petitioners' method of allocating income and expenses to New York on their income tax nonresident returns for the years at issue. The Audit Division regarded all of petitioners' racing, breeding and other farm operations, wherever conducted, as one business and adjusted the amount allocable to New York by the use of a formula in lieu of petitioners' available financial books and records.

16. Petitioners testified that all of the states, other than New York, to which they reported income for tax purposes accepted their method of reporting income and expenses against the income for purposes of determining the net taxable income for the given state.

17. The Audit Division did not offer any rationale for its position nor did it contest the sufficiency of petitioners' financial books and records in determining petitioners' aforementioned tax deficiency.

CONCLUSIONS OF LAW

A. That section 631 of the Tax Law provides in part as follows:

"Section 631. New York taxable income of a nonresident individual. -- (a) General. -- The New York taxable income of a nonresident individual shall be his New York adjusted gross income less his New York deduction and New York personal exemptions..."

B. That section 632 provides in part as follows:

"Section 632. New York adjusted gross income of a nonresident individual. --

(a) General. The New York adjusted gross income of a nonresident individual shall be the sum of the following:

(1) The net amount of items of income, gain, loss and deduction...derived from or connected with New York sources ...

* * *

(b) Income and deductions from New York sources. --

(1) Items of income, gain, loss and deduction derived from or connected with New York sources shall be those items attributable to:

(A) the ownership of any interest in real or tangible personal property in this state; or

(B) a business, trade, profession or occupation carried on in this state." (emphasis added)

C. That from an analysis of sections 631 and 632, in part, it is clear that in order for income of a nonresident individual to be subject to New York income taxes it must be derived from or connected with New York sources, i.e., the income must be attributable to either the ownership of any interest in real or tangible personal property in New York or a business, trade, profession or occupation carried on in New York.

D. That the income derived from petitioners' breeding operations and non-horse related farm operations are clearly not attributable to either the ownership of any interest in real or tangible personal property in New York or any business, trade, profession or occupation carried on in New York.

E. That the New York Court of Appeals has held a taxpayer's return must be accepted as filed if there is no substantial evidence on which to set aside the taxpayer's method of allocating New York income. (Thompson v. Mealey, 290 N.Y. 230). This rationale was further enunciated in Piper, Jaffray & Hopwood v. State Tax Commission, 42 A.D.2d 381, where the Court held the direct accounting method is the preferred method of allocating income between New York and other

jurisdictions and is to be utilized unless the taxpayer's books fail to adequately separate New York income and expenses from non-New York income and expenses.

F. That in view of the above, the question regarding the use of a formula method rather than the petitioners' financial books and records for the purpose of allocating New York income is moot.

G. That the petition herein is granted and the Notice of Deficiency is cancelled.

DATED: Albany, New York

OCT 17 1980

STATE TAX COMMISSION

PRESIDENT

COMMISSIONER

COMMISSIONER