

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition of Estate of J. Stanley Halperin and Florence S. Halperin Cedarbaum	: : : : : :	AFFIDAVIT OF MAILING
for Redetermination of a Deficiency or a Revision of a Determination or a Refund of Personal Income Tax under Article 22 of the Tax Law for the Year 1974.	: : :	

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 4th day of August, 1982, he served the within notice of Decision by certified mail upon Estate of J. Stanley Halperin and Florence S. Halperin Cedarbaum, the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Estate of J. Stanley Halperin
and Florence S. Halperin Cedarbaum
c/o Andrew S. Halperin
285 Madison Ave.
New York, NY 10017

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
4th day of August, 1982.

Conice R. Halperin

J. Vredenburg

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
of	:	
Estate of J. Stanley Halperin	:	
and Florence S. Halperin Cedarbaum	:	AFFIDAVIT OF MAILING
for Redetermination of a Deficiency or a Revision	:	
of a Determination or a Refund of Personal Income	:	
Tax under Article 22 of the Tax Law for the Year	:	
1974.	:	

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 4th day of August, 1982, he served the within notice of Decision by certified mail upon Andrew S. Halperin the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Andrew S. Halperin
285 Madison Ave.
New York, NY 10017

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
4th day of August, 1982.

Annex R. Hayden *J. Vredenburg*

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

August 4, 1982

Estate of J. Stanley Halperin
and Florence S. Halperin Cedarbaum
c/o Andrew S. Halperin
285 Madison Ave.
New York, NY 10017

Mrs. Halperin Cedarbaum:

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 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
Law Bureau - Litigation Unit
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Andrew S. Halperin
285 Madison Ave.
New York, NY 10017
Taxing Bureau's Representative

STATE TAX COMMISSION

Petitioners, the Estate of J. Stanley Halperin and Florence S. Halperin Cedarbaum, c/o Andrew Steven Halperin, Esq., 285 Madison Avenue, New York, New York 10017, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the year 1974 (File No. 20481).

A formal hearing was held before Gasper S. Fasullo, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on February 24, 1981 at 9:15 A.M. Petitioners appeared by Andrew Steven Halperin, Esq. The Audit Division appeared by Ralph J. Vecchio, Esq. (Samuel J. Freund, Esq., of counsel).

I. Whether a loss suffered by a trust may be passed through to and deducted by an income beneficiary of the trust on that beneficiary's personal income tax return if such loss is in excess of the trust's income and if such loss occurs during a year in which the trust does not terminate.

II. Whether, in the event the total amount of the loss suffered by the trust may not be passed through to and deducted by the income beneficiary, any

portion of the loss which is attributable to depreciation may be allocated to and deducted by the income beneficiary.

III. Whether allocation of a partner's distributive share of partnership loss entirely to the year-end owner of the partnership interest may be retroactively changed in order to apportion such loss among the various owners of that partnership interest (based on the various periods of time during which each partner owned the partnership interest during the year).

FINDINGS OF FACT

1. J. Stanley Halperin died on July 30, 1974, leaving a Will, later admitted to probate, by which he created a trust known as the "J. Stanley Halperin Marital Trust" (herein "the Trust"). The sole income beneficiary of the Trust is his wife Florence S. Halperin, now remarried and known by the name of Florence S. Halperin Cedarbaum.

2. At the time of his death J. Stanley Halperin was a limited partner in three (3) different and separate limited partnerships. In December, 1974, the decedant's interest in each of these three (3) limited partnerships was transferred over to the Trust.

3. In its New York State and Federal Fiduciary Returns for the year 1974, the Trust reported no cash distributions from any of the above three (3) partnerships nor any income as having been received, but did report a loss in the amount of \$119,950.00. This entire loss, which represents the Trust's share of losses attributable to its interests in the three (3) limited partnerships, was passed through to Florence S. Halperin as the income beneficiary of the Trust and deducted on petitioners' Federal and New York State Income Tax Returns for 1974.

4. On the New York State income tax return filed for 1974 on behalf of J. Stanley Halperin (up to the time of his death on July 30, 1974) and Florence S. Halperin, taxable income in the amount of \$58,583.00 was reported. As computed by petitioners, this resulted in a New York State income tax liability of \$4,586.00 for the year 1974. Since petitioners had made estimated tax payments totalling \$15,700.00 for the year 1974, petitioners claimed a refund due of \$11,114.00.

5. On July 25, 1977, the Audit Division issued a Statement of Audit Changes and a Notice of Deficiency to petitioners disallowing the deduction of the \$119,950.00 loss and recomputing petitioners' 1974 income tax due as \$21,030.05. After giving petitioners credit for their estimated tax prepayments, the additional tax asserted as due totals \$5,330.05 plus interest.

6. The Trust's pro rata share of the 1974 operating losses incurred by each of the three (3) limited partnerships in which the Trust was a limited partner was computed on the basis of the Trust's percentage of ownership in partnership profits and losses as follows:

<u>Name of Limited Partnership</u>	<u>Partner's % Interest in Partnership Profits and Losses</u>	<u>Partner's Share of 1974 Partnership Losses</u>
a. Central Towers Company	2.639%	\$(31,486.00)
b. Columbus Manor Company	9.000%	\$(33,741.00)
c. Seagirt Houses Associates	2.500%	\$(54,723.00)
Partner's Total Share of Losses...		<u>\$(119,950.00)</u>

7. The portion of the above losses which is attributable to amounts of depreciation allowable to each of the three (3) limited partnerships is computed as follows:

Name of Limited Partnership	Partnership's Total Depreciation	Partner's % Interest Partnership Profits and Losses	Partner's Share of Depreciation
a. Central Towers Company	\$630,553.00	X 2.639%	= \$16,640.29
b. Columbus Manor Company	\$313,832.00	X 9.000%	= \$28,244.88
c. Seagirt Houses Associates	\$541,324.00	X 2.500%	= \$13,533.10
Partner's Total Share of Depreciation...			<u>\$58,418.27</u>

There is no evidence of any provision whereby the Trust, as a partner, would be entitled to receive as part of its distributive share of partnership items of gain, loss, etc., any special allocation of the partnerships' allowable depreciation in excess of the share allocable (as above) in accordance with the partner's percentage interest in partnership profits and losses.

8. Although each of the three (3) limited partnerships, in reporting its overall loss, specifically stated the total of its allowable depreciation for 1974, the pro rata share of such depreciation allocable from each of the partnerships to the Trust, as a partner, was not separately stated to the Trust on Form K-1 ("Partner's Share of Income, Credits, Deductions, etc. - 1974") received by the Trust from each partnership. Each Form K-1 showed simply (at line 1 of Form K-1) the Trust's pro rata share of that partnership's overall loss.

9. On its fiduciary return filed for 1974, the Trust listed the total of its pro rata share of losses received from the three (3) limited partnerships (\$119,950.00), as income from partnerships and other fiduciaries, and passed this entire amount through to Florence S. Halperin as the Trust's sole income beneficiary. No allocation was made between the Trust and its income beneficiary with respect to that portion of the loss which was attributable to depreciation.

10. Among the terms of the Trust, as contained in the Will of J. Stanley Halperin (at Article 9, Paragraph B), was the following provision:

"(B) To determine in their (Executors and Trustees) sole discretion separately with respect to each parcel of real property hereunder, whether or not to set aside a portion of the income from that parcel for the purpose of establishing a reserve fund to compensate for the depreciation, deterioration and obsolescence of such parcel, the amount of said fund to be left entirely to the discretion of my said executors and trustees."

Although this provision allowed the establishment of a reserve fund for depreciation of Trust property, no such fund was in fact set up by the trustees in 1974.

CONCLUSIONS OF LAW

A. That "...a trust is deemed an entity separate and distinct from its beneficiaries, and any operating loss suffered is that of the trust and not that of its beneficiaries." Kearney v. U.S., 116 F. Supp. 922,925 (S.D.N.Y. 1953). However, upon the termination of a trust certain loss carryovers and or excess deductions of a trust may be allowed as deductions to the beneficiaries succeeding to the property of the trust (Internal Revenue Code §642(h)). Accordingly, since the J. Stanley Halperin Marital Trust (the "Trust") did not terminate in 1974, the total loss sustained by the Trust may not properly be passed through from the Trust to Florence S. Halperin as the Trust's income beneficiary.

B. That section 642(e) of the Internal Revenue Code in pertinent part provides:

"... [a]n estate or trust shall be allowed the deduction for depreciation... only to the extent not allowable to beneficiaries under section 167(h)..."

Furthermore, section 167(h) of the Internal Revenue Code in pertinent part provides:

"(h) Life Tenants and Beneficiaries of Trusts and Estates. ... In the case of property held in trust, the allowable deduction shall be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income allocable to each....". (emphasis added).

C. That Treasury Regulation section 1.167(h)-1(b) provides:

"(b) Trusts. If property is held in trust, the allowable deduction is to be apportioned between the income beneficiaries and the trustee on the basis of the trust income allocable to each, unless the governing instrument (or local law) requires or permits the trustee to maintain a reserve for depreciation in any amount. In the latter case, the deduction is first allocated to the trustee to the extent that income is set aside for a depreciation reserve, and any part of the deduction in excess of the income set aside for the reserve shall be apportioned between the income beneficiaries and the trustee on the basis of the trust income (in excess of the income set aside for the reserve) allocable to each..."

D. That section 702(a)(8) of the Internal Revenue Code requires a partner to account separately for his distributive share of certain partnership items of gain, loss, deduction, or credit as specified in the regulations pertaining to section 702(a)(8). Revenue Ruling 74-71 (1974-1 C.B. 158) explains inter alia the inter-relationship of Internal Revenue Code sections 702(a)(8) and 167(h) where a trust is a member of a partnership by providing, in pertinent part:

"Section 1.702-1(a)(8) of the regulations provides, in pertinent part, that each partner shall take into account separately, any items of income, gain, loss, deduction, or credit subject to a special allocation under the partnership agreement which differs from the allocation of partnership taxable income or loss generally and any partnership item which if separately taken into account by any partner would result in an income tax liability for that partner different from that which would result if that partner did not take the item into account separately.

Accordingly, where under the provisions of section 167(h)... of the Code, the depreciation... deduction... in the case of the trust are (sic) allowable to its beneficiaries, and where such deductions if separately taken into account by the... trust would result in an income tax liability for the... trust different from that which would result if the... trust did not take such deductions into account separately, then the depreciation ... of property held by any partnership in which the... trust is a partner must be taken into account separately by the... trust under the rules contained in section 702(a)(8) of the regulations pertaining thereto." (emphasis added). See also 47 ALR Fed. 537 at 547.

E. That since there was no special allocation of depreciation to the Trust by any of the partnerships (Finding of Fact "7") and since separate accounting for depreciation in this case would not effect any change in the Trust's income tax liability (income tax liability would remain at \$0.), the Trust is not required to separately account for its distributive share of the partnerships' allowable depreciation.¹

F. That there are no trust provisions directing apportionment of depreciation between the Trust and its beneficiary, and no income was set aside by the trustee as a reserve fund for depreciation (despite the trustees' authority, in their discretion, to establish such a fund). Accordingly, since all Trust income was allocable annually to Florence S. Halperin as the Trust's sole income beneficiary, she is entitled to the entire amount of depreciation

¹ "43. See Rev. Rul. 74-71, 1974-1 C.B. 158, holding that since depreciation or depletion of a trust or estate must be allocated between the trust or estate and its beneficiaries, these items must be separately stated under §702(a)(8) (now §702(a)(7)), if separate statement would result in a difference in the tax liability of the estate or trust. Although it is not entirely clear from the ruling, it seems that separate statement is not required under §702(a)(7) if the only effect of the separate statement would be on the tax liability of the beneficiary (who is not a partner) rather than the estate or trust (which might pay no tax because of losses or distributions)..." (McKee, Nelson, Whitmire; Federal Taxation of Partnerships and Partners., Vol. 1, ¶9.03[2] note 43.) (emphasis added).

distributed by the three (3) limited partnerships to the Trust. Furthermore, the entire amount of depreciation is to be allocated to the beneficiary (Florence S. Halperin) even though this amount exceeds the amount of income distributed and, in fact, even though there was no trust income to be distributed. See Matter of Sue Carol, 30 BTA 443, and Matter of Edna C. Gutman, 1 T.C. 365, aff'd 143 F2d 201.

G. That based on the foregoing, petitioners may not deduct the entire loss reported by the Trust (\$119,950.00), but may properly deduct so much of that loss as was due to depreciation (\$58,418.27; see Finding of Fact "7").

H. That the partner's distributive shares of losses incurred in 1974 by the three (3) limited partnerships were allocated entirely to the Trust, (as the decedant's successor in interest) rather than apportioned between J. Stanley Halperin (deceased) and the Trust based on the respective portions of the year (1974) during which each was a partner. In cases of death of a partner, such allocation (rather than apportionment between the decedant and his successor in interest) is proper within the meaning and intent of section 706(c) of the Internal Revenue Code and regulations thereunder. (McKee, Nelson, Whitmire; Federal Taxation of Partnerships and Partners., ¶ 23.01 [1] and authority cited therein.).

I. That the petition of the Estate of J. Stanley Halperin (deceased) and Florence S. Halperin Cedarbaum is granted to the extent indicated in Conclusion of Law "G". The Audit Division is directed to recompute petitioners' 1974 tax

liability in accordance therewith, and that the petition is in all other respects denied.

DATED: Albany, New York

AUG 04 1982

STATE TAX COMMISSION

ACTING

PRESIDENT

COMMISSIONER

COMMISSIONER