

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition :  
of :  
Traveler Trading Co. :  
for Redetermination of a Deficiency or for Refund :  
of Unincorporated Business Tax under Article 23 of :  
the Tax Law for the Fiscal Year Ended June 25, :  
1976. :

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In the Matter of the Petition :  
of :  
Sara Spiegler :  
for Redetermination of a Deficiency or for Refund :  
of New York State Personal Income Tax under Article :  
22 of the Tax Law and New York City Nonresident :  
Earnings Tax under Chapter 46, Title U of the :  
Administrative Code of the City of New York for :  
the Years 1976 and 1977. :

AFFIDAVIT OF MAILING

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In the Matter of the Petition :  
of :  
Gary Spiegler :  
for Redetermination of a Deficiency or for Refund :  
of New York State Personal Income Tax under Article :  
22 of the Tax Law for the Year 1976, New York State :  
Personal Income and Unincorporated Business Taxes :  
under Articles 22 and 23 of the Tax Law for the :  
Year 1977, and New York City Nonresident Earnings :  
Tax under Chapter 46, Title U of the Administrative :  
Code of the City of New York for the Years 1976 and :  
1977. :

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State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 13th day of September, 1985, he served the within notice of Decision by certified mail upon Gary Spiegler, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Gary Spiegler  
5 Pumpkin Hill  
Westport, CT 06880

Page 2

Affidavit of Mailing

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office 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  
13th day of September, 1985.

David Parchuck

William A. Haywood  
Authorized to administer oaths  
pursuant to Tax Law section 174

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

September 13, 1985

Gary Spiegler  
5 Pumpkin Hill  
Westport, CT 06880

Dear Mr. Spiegler:

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 & 1312 of the Tax Law and Chapter 46, Title U of the Administrative Code of the City of New York, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only 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  
Ronald Nadler  
Rick Minty & Nadler  
10 E. 40th St. - Room 906  
New York, NY 10016  
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

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State of New York :

ss.:

County of Albany :

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Page 2

Affidavit of Mailing

Ronald Nadler  
Rick Mintz & Nadler  
10 E. 40th Street - Room 906  
New York, NY 10016

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office 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  
13th day of September, 1985.

David Parchuck

Caroline DeGelman  
Authorized to administer oaths  
pursuant to Tax Law section 174

STATE OF NEW YORK

STATE TAX COMMISSION

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Sara Spiegler  
5 Pumpkin Hill  
Westport, CT 06880

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Affidavit of Mailing

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David Parchuck

Annunzio D. Vagelburg

Authorized to administer oaths  
pursuant to Tax Law section 174

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

September 13, 1985

Sara Spiegler  
5 Pumpkin Hill  
Westport, CT 06880

Dear Ms. Spiegler:

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

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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  
Ronald Nadler  
Rick Mintz & Nadler  
10 E. 40th Street - Room 906  
New York, NY 10016  
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

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Traveler Trading Co.  
c/o Rick, Mintz & Nadler  
10 E. 40th Street, Room 906  
New York, NY 10016

Page 2

Affidavit of Mailing

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Sworn to before me this  
13th day of September, 1985.

David Parcluck

Ann O'Hanlon

Authorized to administer oaths  
pursuant to Tax Law section 174

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

September 13, 1985

Traveler Trading Co.  
c/o Rick, Mintz & Nadler  
10 E. 40th Street, Room 906  
New York, NY 10016

Gentlemen:

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, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only 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.

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Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative  
Ronald Nadler  
Rick, Mintz & Nadler  
10 East 40th St., Room 906  
New York, NY 10016  
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition  
of  
TRAVELER TRADING CO.  
for Redetermination of a Deficiency or for  
Refund of Unincorporated Business Tax under  
Article 23 of the Tax Law for the Fiscal Year  
Ended June 25, 1976.

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In the Matter of the Petition  
of  
SARA SPIEGLER  
for Redetermination of a Deficiency or for  
Refund of New York State Personal Income Tax  
under Article 22 of the Tax Law and New York  
City Nonresident Earnings Tax under Chapter 46,  
Title U of the Administrative Code of the City  
of New York for the Years 1976 and 1977.

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DECISION

In the Matter of the Petition  
of  
GARY SPIEGLER  
for Redetermination of a Deficiency or for  
Refund of New York State Personal Income Tax  
under Article 22 of the Tax Law for the Year  
1976, New York State Personal Income and  
Unincorporated Business Taxes under Articles 22  
and 23 of the Tax Law for the Year 1977, and  
New York City Nonresident Earnings Tax under  
Chapter 46, Title U of the Administrative Code  
of the City of New York for the Years 1976 and  
1977.

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Petitioner, Traveler Trading Co., c/o Rick, Mintz & Nadler, 10 East 40th  
Street, Room 906, New York, New York 10016, filed a petition for redetermination

of a deficiency or for refund of unincorporated business tax under Article 23 of the Tax Law for the fiscal year ended June 25, 1976 (File No. 30982).

Petitioner, Sara Spiegler, 5 Pumpkin Hill, Westport, Connecticut 06880, filed a petition for redetermination of a deficiency or for refund of New York State personal income tax under Article 22 of the Tax Law and New York City nonresident earnings tax under Chapter 46, Title U of the Administrative Code of the City of New York for the years 1976 and 1977 (File No. 30980).

Petitioner, Gary Spiegler, 5 Pumpkin Hill, Westport, Connecticut 06880, filed a petition for redetermination of a deficiency or for refund of New York State personal income tax under Article 22 of the Tax Law for the year 1976, New York State personal income and unincorporated business taxes under Articles 22 and 23 of the Tax Law for the year 1977, and New York City nonresident earnings tax under Chapter 46, Title U of the Administrative Code of the City of New York for the years 1976 and 1977 (File Nos. 31395, 31396 and 31397).

A formal hearing was commenced before Arthur Bray, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on August 9, 1983 at 10:20 A.M., continued at the same offices on May 10, 1984 at 1:15 P.M. and concluded at the same offices on July 31, 1984 at 10:30 A.M., with all briefs to be submitted on or before December 31, 1984. Petitioner appeared by Rick, Mintz & Nadler, P.C. (Joseph Rick, C.P.A. and Ronald J. Nadler, C.P.A.). The Audit Division appeared by John P. Dugan, Esq. (Kevin A. Cahill, Esq., of counsel).

#### ISSUES

I. Whether the Audit Division properly determined that Traveler Trading Co. is liable for additional unincorporated business tax.

II. Whether the Audit Division properly determined that Sara Spiegler is liable for additional New York State personal income tax and New York City nonresident earnings tax.

III. Whether the Audit Division properly determined that Gary Spiegler was liable for additional personal income tax for the years 1976 and 1977, unincorporated business tax for the year 1977 and New York City nonresident earnings tax for the years 1976 and 1977.

FINDINGS OF FACT

1. Petitioner Traveler Trading Co. filed a New York State Partnership Return for the period January 1, 1976 through June 25, 1976.

2. Petitioner Sara Spiegler filed New York State income tax nonresident returns and nonresident earnings tax returns for the City of New York for the years 1976 and 1977.

3. Petitioner Gary Spiegler filed New York State income tax nonresident returns and nonresident earnings tax returns for the City of New York for the years 1976 and 1977. He did not file a New York State Unincorporated Business Tax Return for the year 1977.

4. On July 24, 1980, the Audit Division issued a Notice of Deficiency to petitioner Traveler Trading Co. asserting a deficiency of unincorporated business tax for the fiscal year ended June 25, 1976 in the amount of \$4,400.32, plus penalty and interest of \$1,482.76, for a total amount due of \$5,883.08. The Statement of Unincorporated Business Tax Audit Changes explained that the asserted deficiency of unincorporated business tax was premised upon the disallowance of purchases which were overstated due to an embezzlement. The Statement further explained that an embezzlement loss is deductible only in the year of discovery and that the amount of the loss must be reduced by the amount

of anticipated recovery. The amount of the disallowed purchases of \$80,000.00 was distributed in equal shares to the partners of Traveler Trading Co. - Gary Spiegler and Sara Spiegler. The penalty was asserted pursuant to section 685(c) of the Tax Law for underpayment of estimated tax.

5. On July 24, 1980, the Audit Division issued a Notice of Deficiency to Sara Spiegler asserting a deficiency of New York State personal income tax and New York City nonresident earnings tax for the years 1976 and 1977 in the amount of \$6,935.87, plus penalty and interest of \$1,949.50, for a total amount due of \$8,885.37. For the year 1976, the Audit Division increased Sara Spiegler's distributive share of partnership income by \$40,000.00 as a result of the disallowed purchases described in Finding of Fact "4", supra. For the years 1976 and 1977, the Audit Division increased Sara Spiegler's distributive share of partnership income from the partnership known as 35-37 West 23rd Street Associates in the amounts of \$4,948.83 and \$2,995.54, respectively. The increase in the distributive share of partnership income arose from adjusting the useful life utilized by 35-37 West 23rd Street Associates to compute the depreciation on the building owned by it from five and one-half years and eight years, which were utilized for the years 1976 and 1977, to thirty years. For the year 1977, the Audit Division increased Sara Spiegler's distributive share of partnership income from the partnership of Colt, Park Associates by \$252.00 based upon an examination of the Colt, Park Associates partnership return.

6. On July 24, 1980, the Audit Division issued a Notice of Deficiency to Gary Spiegler asserting a deficiency of New York State personal income tax and New York City nonresident earnings tax for the year 1976 in the amount of \$9,156.77, plus interest of \$2,586.04, for a balance due of \$11,742.81. The

Notice of Deficiency was premised upon increasing Gary Spiegler's distributive share of partnership income by \$40,000.00 as a result of the disallowed purchases described in Finding of Fact "4", supra. The Audit Division also increased said petitioner's distributive share of partnership income from 35-37 West 23rd Street Associates by \$12,249.17 based upon the adjustment to the useful life of the building and the Audit Division's understanding that Gary Spiegler had an approximately 71 percent interest in 35-37 West 23rd Street Associates. The Audit Division also attributed \$8,164.00 of commission income to Gary Spiegler for 1976 arising from petitioner's income from Muncie Novelty Co., Inc. ("Muncie"). In reaching this determination, the Audit Division concluded that Gary Spiegler did not have a place of business outside New York and that he was conducting business within New York.

7. On July 24, 1980, the Audit Division issued a Notice of Deficiency to Gary Spiegler asserting a deficiency of New York State personal income tax and New York City nonresident earnings tax for the year 1977 in the amount of \$1,939.69, plus interest of \$403.25, for a total amount due of \$2,342.94. The Statement of Personal Income Tax Audit Changes explained that the asserted deficiency was premised upon several adjustments. First, the Audit Division attributed to Mr. Spiegler additional income of \$7,414.00 arising from the adjustment to the useful life of the building utilized by 35-37 West 23rd Street Associates. The Audit Division also disallowed a reported loss of \$4,301.00 from Can-Am Drilling Programs since it was not documented that the loss was properly allocated to New York. The Audit Division also attributed \$14,298.00 of additional commission income from Muncie. Lastly, the Audit Division modified Mr. Spiegler's reported computation of the allocation of wages to New York as follows:

|                           | <u>Reported</u> | <u>Adjusted</u> |
|---------------------------|-----------------|-----------------|
| Total days worked in year | 342             | 301             |
| Days worked outside N.Y.  | 229             | 190             |
| Days worked in N.Y.       | 113             | 111             |

No information was presented to explain the basis for the change in the total days worked in the year.

8. On July 24, 1980, the Audit Division issued a Notice of Deficiency to Gary Spiegler asserting a deficiency of unincorporated business tax for the year 1977 in the amount of \$305.11, plus penalty and interest of \$171.74, for a total amount due of \$476.85. The asserted deficiency was premised upon the Audit Division's conclusion that Gary Spiegler's income from Muncie was subject to unincorporated business tax. The penalties were asserted pursuant to sections 685(a)(1) and 685(a)(2) of the Tax Law for, respectively, failure to file an unincorporated business tax return and failure to pay amounts shown as tax on a return required to be filed.

9. Traveler Trading Co. ("Trading Co.") was a partnership which engaged in the importation and domestic sale of Halloween and novelty items. Sara Spiegler and Gary Spiegler were equal partners of Trading Co. until June 25, 1976. Thereafter, the assets and liabilities of Trading Co. were transferred to Traveler Trading Co., Inc. and stock ownership was held equally by Sara Spiegler and Gary Spiegler.

10. During the years 1975, 1976 and 1977, Trading Co. and its successor, Traveler Trading Co., Inc., sustained embezzlement losses arising from actions taken by its bookkeeper. The embezzled funds were concealed by adding the amount embezzled to Trading Co.'s purchases account. In order to determine the amount of the embezzlement, Mr. Speigler showed the Audit Division copies of

bank checking account statements. Circled amounts thereon indicated the amounts that were embezzled and, hence, the amounts by which purchases were overstated.

11. The embezzlement loss was discovered in March or April, 1977. On or about June 20, 1977, Trading Co. and Traveler Trading Co., Inc. commenced a lawsuit against Chase Manhattan Bank and an accounting firm in the amount of \$300,000.00 to recover the losses sustained as a result of the embezzlement. In 1984, plaintiffs received \$105,000.00 for the defalcation loss sustained in 1975 and defendants were issued a general release from subsequent litigation on this complaint.

12. The partnership of 35-37 West 23rd Street Associates was a firm whose business activity consisted of ownership of a building. The building was built in 1879 and contained an antiquated hand-operated elevator. The first floor of the building contained a store. Approximately one-third of the second floor was used as an office. The balance of the second floor, as well as the third and fourth floors, were used for storage. The higher floors of the building were tested and found to be weak. In determining the useful life of the building for the reported computation of depreciation, 35-37 West 23rd Street Associates took into account the age of the building and a letter from an engineer concerning the condition of the building.

13. Gary Spiegler and Sara Spiegler each had a fifty percent interest in 35-37 West 23rd Street Associates. However, the reported depreciation expense of the building was not the same for each partner since they acquired their shares of the partnership at different times and reported different cost bases for depreciation.

14. The Audit Division concluded that Sara Spiegler had additional income from Colt, Park Associates in 1977 based upon an examination of the Colt, Park Associates partnership return. However, the Audit Division was unable to explain why this income was considered subject to New York State tax.

15. Prior to the periods in issue, Gary Spiegler developed customer accounts from the sale of carnival and ride tickets for Muncie. During the periods in issue, these customers continued to place orders with Muncie without contacting Gary Spiegler. Muncie, in turn, would mail a commission check to Gary Spiegler either at his home in Connecticut or at Trading Co., depending upon the location of the customer. That is, if the company that ordered the tickets was located outside of New York State, the commission checks would be sent to Gary Spiegler at his home in Connecticut. If a company located in New York ordered tickets from Muncie, the commission checks would be sent to Trading Co.

16. Gary Spiegler's business activity at home with respect to Muncie consisted of receiving checks and drafting deposit slips. His accountant prepared Mr. Spiegler's tax returns allocating the commission income on the basis of what Mr. Spiegler told him.

17. Gary Spiegler maintained an itinerary of the number of days worked within and without New York State. This itinerary was used by Mr. Spiegler's accountant to determine the reported allocation of wages. Although this itinerary was available for inspection at the time of the audit, it was not provided since the topic of allocation of wages was not broached during the audit.

CONCLUSIONS OF LAW

A. That the New York adjusted gross income of a nonresident individual is the sum of "[t]he net amount of items of income, gain, loss and deduction entering into his federal adjusted gross income, as defined in the laws of the United States for the taxable year derived from or connected with New York sources..." with certain modifications [Tax Law §632(a)(1)].

B. That losses arising from theft are deductible pursuant to section 165(a) of the Internal Revenue Code [Treas. Reg. §1.165-8(a)(1)]. The term "theft" is deemed to include "embezzlement" [Treas. Reg. §1.165-8(d)].

C. That Treas. Reg. §1.165-8(a)(2) provides:

"A loss arising from theft shall be treated under section 165(a) as sustained during the taxable year in which the taxpayer discovers the loss. See section 165(e). Thus, a theft loss is not deductible under section 165(a) for the taxable year in which the theft actually occurs unless that is also the year in which the taxpayer discovers the loss. However, if in the year of discovery there exists a claim for reimbursement with respect to which there is a reasonable prospect of recovery, see paragraph (d) of § 1.165-1." (emphasis added).

D. That since the embezzlement loss was not discovered until 1977, the Audit Division properly concluded that the embezzlement loss was not deductible in 1976 [Treas. Reg. §1.165-8(a)(2)].

E. That Treas. Reg. §1.165-1(d)(3) provides:

"Any loss arising from theft shall be treated as sustained during the taxable year in which the taxpayer discovers the loss (see § 1.165-8, relating to theft losses). However, if in the year of discovery there exists a claim for reimbursement with respect to which there is a reasonable prospect of recovery, no portion of the loss with respect to which reimbursement may be received is sustained, for purposes of section 165, until the taxable year in which it can be ascertained with reasonable certainty whether or not such reimbursement will be received." (emphasis added).

F. That assuming that the partnership of Traveler Trading Co. continued to exist for tax purposes in 1977, Gary Spiegler and Sara Spiegler would not have been entitled to deduct the embezzlement losses on their respective

personal income tax returns, since there existed at that time a reasonable prospect for recovery, as evidenced by the lawsuit against Chase Manhattan Bank and the accounting firm.

G. That in determining the useful life of an asset, Treas. Reg. §1.167(a)-1(b) provides, in part, as follows:

"(b) Useful life. For the purpose of section 167 the estimated useful life of an asset is not necessarily the useful life inherent in the asset but is the period over which the asset may reasonably be expected to be useful to the taxpayer in his trade or business or in the production of his income. This period shall be determined by reference to his experience with similar property taking into account present conditions and probable future developments. Some of the factors to be considered in determining this period are (1) wear and tear and decay or decline from natural causes, (2) the normal progress of the art, economic changes, inventions, and current developments within the industry and the taxpayer's trade or business, (3) the climatic and other local conditions peculiar to the taxpayer's trade or business, and (4) the taxpayer's policy as to repairs, renewals, and replacements."

H. That in view of the age, condition and use of the building owned by 35-37 West 23rd Street Associates, petitioners have established that the useful life that they ascribed to the building for purposes of computing depreciation was reasonable under the circumstances.

I. That Sara Spiegler has failed to sustain her burden of proof of establishing that the income from Colt, Park Associates was not subject to New York State personal income tax [Tax Law §689(e)].

J. That based upon all of the facts and circumstances presented, Gary Spiegler has sustained his burden of proof of establishing that his allocation of wage income was proper [Tax Law §689(e)]. Accordingly, the portion of the Notices of Deficiency issued to Gary Spiegler based upon the adjustment to petitioner's allocation of wages within and without New York State is cancelled.

K. That Gary Spiegler has not sustained his burden of proof of establishing that the loss from Can-Am Drilling Programs was properly allocated to New York [Tax Law §689(e)].


L. That since the income received by Traveler Trading Co. from Muncie was the result of Gary Spiegler's efforts, and since Gary Spiegler did not maintain an office at his home in Connecticut with respect to his commission generating activities from Muncie, it must be concluded that the only office maintained by Gary Spiegler with respect to this income was in New York at the offices of Traveler Trading Co. Accordingly, the Audit Division properly concluded that Gary Spiegler's income from Muncie was subject to New York State personal income tax and unincorporated business tax (Tax Law §§632(c), 707(a)).

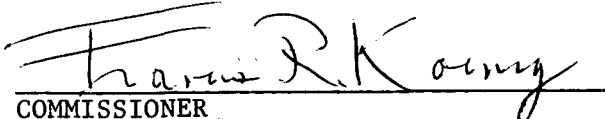
M. That the petition of Traveler Trading Co. is granted to the extent of Conclusion of Law "H"; that the petition of Sara Spiegler is granted to the extent of Conclusion of Law "H"; that the petition of Gary Spiegler is granted to the extent of Conclusions of Law "H" and "J"; that the Audit Division is directed to modify the notices of deficiency in accordance herewith; and that except to the extent that the petitions are granted above, the notices of deficiency are sustained.


DATED: Albany, New York

STATE TAX COMMISSION

SEP 13 1985

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER