

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Estates of Ralph & Charles Abrams :
for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Unincorporated :
Business Tax under Article 23 of the Tax Law for :
the Years 1969 - 1976. :
:

AFFIDAVIT OF MAILING

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 29th day of May, 1985, he served the within notice of Decision by certified mail upon Estates of Ralph & Charles Abrams, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Estates of Ralph & Charles Abrams
c/o Goldschmidt, Fredericks & Oshatz
655 Madison Ave.
New York, NY 10021

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
29th day of May, 1985.

David Parchuck

Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

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of :
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Business Tax under Article 23 of the Tax Law for :
the Years 1969 - 1976. :
:

AFFIDAVIT OF MAILING

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 29th day of May, 1985, he served the within notice of Decision by certified mail upon Leonard A. Messinger, the representative of the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Leonard A. Messinger
Goldschmidt, Fredericks & Oshatz
655 Madison Ave.
New York, NY 10021

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
29th day of May, 1985.

David Parchuck

Authorized to administer oaths
pursuant to Tax Law section 174

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

May 29, 1985

Estates of Ralph & Charles Abrams
c/o Goldschmidt, Fredericks & Oshatz
655 Madison Ave.
New York, NY 10021

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.

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
Leonard A. Messinger
Goldschmidt, Fredericks & Oshatz
655 Madison Ave.
New York, NY 10021
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
	:	
of	:	
	:	
ESTATE OF RALPH ABRAMS and	:	DECISION
ESTATE OF CHARLES ABRAMS	:	
	:	
for Redetermination of a Deficiency or for	:	
Refund of Unincorporated Business Tax under	:	
Article 23 of the Tax Law for the Years 1969	:	
through 1976.	:	

Petitioners, Estate of Ralph Abrams and Estate of Charles Abrams, c/o Goldschmidt, Fredericks & Oshatz, Esqs., 655 Madison Avenue, New York, New York 10021, filed a petition for redetermination of a deficiency or for refund of unincorporated business tax under Article 23 of the Tax Law for the years 1969 through 1976 (File No. 26170).

A formal hearing was held before Robert A. Couze, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on February 10, 1983 at 1:30 P.M., with all briefs submitted by May 27, 1983. Petitioners appeared by Goldschmidt, Fredericks & Oshatz, Esqs. (Barry I. Fredericks, Esq. and Leonard A. Messinger, Esq., of counsel). The Audit Division appeared by Paul B. Coburn, Esq. (Anne W. Murphy, Esq., of counsel).

On February 10, 1983, Barry I. Fredericks, on behalf of petitioners, and Anne W. Murphy, on behalf of the Audit Division, executed a stipulation of facts which included seven exhibits appended thereto and made a part thereof. The facts agreed upon and excerpts from the exhibits are set forth in the Findings of Fact, infra.

ISSUES

I. Whether the notices of deficiency issued to the partnership Ralph and Charles Abrams for the years 1969 through 1974 were barred by the time limitations on assessment set forth in section 683 of the Tax Law.

II. Whether income derived from the real estate activities of the partnership was subject to unincorporated business tax.

III. Whether the Audit Division properly asserted against the partnership additions to tax pursuant to sections 685(a)(1) and 685(a)(2) of the Tax Law.

FINDINGS OF FACT

1. Ralph and Charles Abrams is a New York general partnership which began business on August 17, 1944. The partners were Ralph Abrams and Charles Abrams, who were brothers.

2. The partnership has filed tax returns with the Federal government and the New York State government on a calendar year basis for each year since 1944. The New York partnership returns for 1969 and 1973 through 1976 listed the type of business as "Real Estate", while the returns for 1970, 1971 and 1972 listed the type of business as "Real Estate Investment". At Schedule U-D, Unincorporated Business Tax and Payments, of the New York partnership returns for 1969 through 1974, the preparer entered "exempt"; on the returns for 1975 and 1976, such schedule was left blank. The returns for 1969 through 1974 included attached schedules which identified the sources of all income received.

3. On June 7, 1978, the Audit Division issued to the estate of Ralph Abrams, Sara K. Abrams, executrix, and the estate of Charles Abrams, Henry J. Goldschmidt, executor, individually and as co-partners doing business under the firm name and style of Abrams and Abrams (sic) two statements of audit changes,

proposing to subject to unincorporated business tax income from the partnership's real estate activities and asserting interest and penalties, as follows:

	<u>1969</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>	
Ordinary income	\$ 73,456.36	\$ 31,176.27	\$ 31,201.31	\$ 65,680.41	
Qualifying dividends	74,277.75	76,776.52	85,616.82	57,099.20	
Short-term capital gains or (losses)	(39,649.65)	--	--	--	
Long-term capital gains or (losses)	38,637.68	1,626.67	--	--	
Total	\$146,722.14	\$109,579.46	\$116,818.13	\$122,779.61	
Less contributions	2,285.00	190.00	--	--	
Balance	\$144,437.14	\$109,389.46	\$116,818.13	\$122,779.61	
Allowance for partners' services	10,000.00	10,000.00	5,000.00	--	
Exemption	5,000.00	5,000.00	5,000.00	5,000.00	
Taxable business income	\$129,437.14	\$ 94,389.46	\$106,818.13	\$117,779.61	
Unincorporated business tax	\$ 7,119.04	\$ 5,191.42	\$ 5,875.00	\$ 6,477.88	\$24,663.34
Interest					10,371.95
Penalties under sections 685(a)(1) and 685(a)(2)	3,381.54	2,465.92	2,790.63	3,076.99	11,715.08
					<u>\$46,750.37</u>
	<u>1973</u>	<u>1974</u>	<u>1975</u>	<u>1976</u>	
Ordinary income	\$ 95,002.24	\$ 84,277.43	\$ 52,016.00	\$ 45,685.00	
Qualifying dividends	71,846.75	84,304.96	76,596.00	66,898.00	
Long-term capital gains or (losses)	--	30,606.34	--	--	
Unclassified income	19,189.71	--	--	--	
Sales or exchanges of property	--	--	--	47,220.00	
Total	\$186,038.70	\$199,188.73	\$128,612.00	\$156,803.00 *	
Exemption	5,000.00	5,000.00	5,000.00	5,000.00	
Taxable business income	\$181,038.70	\$194,188.73	\$123,612.00	\$151,803.00	
Unincorporated business tax	\$ 9,957.13	\$ 10,680.38	\$ 6,798.66	\$ 8,349.17	\$35,785.34
Interest					8,003.24
Penalties under sections 685(a)(1) and 685(a)(2)					14,038.52
					<u>\$57,827.10</u>

* An arithmetical error was made in arriving at the total; total income should be \$159,803.00.

On December 15, 1978, the Audit Division issued to the partnership two notices of deficiency, asserting unincorporated business tax due for the years 1969

through 1976 in the amounts above-stated and recomputing the interest and penalties to the date of the issuance of the notices.

4. The partnership has been engaged solely in the real estate business. It has not engaged in any form of business other than owning, operating or managing real property. As reflected in the partnership's tax returns, its income for 1969 through 1976 was derived from the following sources: (a) net income from rentals of property wholly owned by the partnership; (b) net income from other partnerships and joint ventures in which the partnership was a participant and whose activities consisted of the rental of property; (c) net income from management of real estate; (d) capital gains (or losses) on sales of securities; (e) gain on the sale or exchange of property used in the trade or business (section 1231 property); and (f) interest earned on bank accounts and deposits of funds.

5. Turtle Bay Theatre Corporation ("Turtle Bay") was a corporation whose sole shareholders were the partnership and Donald Rugoff. In 1961, Turtle Bay purchased a long-term ground lease at 1001-1007 Third Avenue, New York, New York, on which premises it caused a motion picture theater to be constructed and operated. Some of the money for this venture was supplied by the partnership, some by friends of Ralph Abrams and Charles Abrams, some by a group headed by Rugoff, and some through the Rugoff & Becker Management Corporation ("Management"), a corporation owned or controlled by Rugoff. Approximately one-half of the money was supplied by the Rugoff-related entities, and the remainder was supplied by the Abrams group.

On February 8, 1961, Turtle Bay entered into an agreement with Management and Hara Construction Co., Inc. ("Hara"), a corporation owned entirely by the partnership, in which the real estate and theater management responsibilities

were delineated. Management was named managing agent, with duties covering the conduct of the theater business, including buying and booking films for exhibition, employing all necessary personnel and performing and discharging all obligations of the tenant under the ground lease. Hara was named building agent with the duty of performing general real estate services. Paragraph Third of the agreement further defined the building agent's responsibilities as follows:

"The Building Agent shall consult and advise the Owner with respect to all matters affecting the real estate and improvements thereon, including but not limited to the construction and maintenance of buildings and improvements, obtaining and refinancing any mortgages thereon, rental of non-theatre premises, and real estate taxes."

Under the terms of the agreement, Hara had the right to designate certain parties to perform the services required of the building agent and to receive the fees therefor.

"The Building Agent may designate Ralph Abrams and/or Charles Abrams or any firm, partnership or corporation owned or controlled by them or either of them or their spouses or issue to perform the services required of the Building Agent hereunder and to receive the fee for such services. Such designation shall be in writing, shall state the designee agrees to be bound by all the terms and conditions of this Agreement and shall be signed by the Building Agent and the designee, and shall be delivered or sent by registered mail to the Owner, copy to the Managing Agent."

At the time the agreement was executed, Charles Abrams's two daughters were minors.

Effective January 1, 1969, Hara designated Ralph Abrams as "building agent" and to receive the fees allocated thereto. All payments made to Ralph Abrams were deposited to the account of Ralph and Charles Abrams and were deemed income of the partnership.

6. Hara, the partnership, Ralph Abrams or Charles Abrams never performed any services for Turtle Bay. The language of the 1961 agreement requiring the performance of services as building agent was, in the understanding of the

parties to that agreement, merely a device to enable sums to be paid to Ralph Abrams and Charles Abrams in excess of that to which they would have been entitled in accordance with their proportionate share of the capital investment.

7. The Estate of Ralph Abrams continued to receive fees under the 1961 agreement after his death on August 15, 1971.

8. On May 11, 1959, the partnership entered into a separate, independent joint venture transaction with Rugoff Theatres, Inc. The joint venture acquired the Murray Hill Theatre, located at 160-64 East 34th Street, New York, New York, in the name of Murray Hill Theatre Corporation and leased the property to 34th Street Theatre Corporation, which was to operate the theater. By agreement dated June 2, 1959, Management was to receive a five percent commission for operating the property.

9. In 1969, a dispute arose between Ralph and Charles Abrams and Rugoff which resulted in litigation and ultimately an arbitration hearing. The litigation revolved around the question whether Ralph Abrams and Charles Abrams were entitled to be offered the right to participate in an offering of stock made by Rugoff at the same price as the stock was initially offered to the public. The matter was settled on June 23, 1969. On the same date and in furtherance of the settlement of the litigation, an agreement was entered into between Charles Abrams and Ralph Abrams and Rugoff allowing that one percent out of the five percent fee received by Rugoff would be paid to Charles Abrams and Ralph Abrams effective as of January 1, 1959:

"Rugoff Theatres, Inc. hereby agrees to pay jointly to Charles Abrams and Ralph Abrams one fifth (1/5) of any fee which Rugoff Theatres, Inc. shall receive pursuant to the Management Agreement dated June 2, 1959 for managing the Murray Hill Theatre whether under the present management agreement, any future agreement or on any other basis for services as "Building Agent", including consultation and advice with respect to all matters affecting the real estate and improvements of the Murray Hill Theatre, including but not limited to the construction

and maintenance of buildings and improvements, obtaining and refinancing any mortgages thereon, rental of non-theatre premises, and real estate taxes. It is understood that said one fifth (1/5) of Rugoff Theatres, Inc.'s fee is presently equal to one percent (1%) of the gross receipts derived from the Murray Hill Theatre as defined in said Management Agreement. Said payments shall commence as of January 1, 1969 and continue so long as Rugoff Theatres, Inc. or any successor manages the Murray Hill Theatre and so long as Charles Abrams, Ralph Abrams, their spouses, issue, heirs or any corporation, firm or partnership controlled by them, or any of them in the aggregate shall own at least 15½% of the stock of the Murray Hill Theatre Corp. and 15½% of the Joint Venture, dated June 10, 1959."

The agreement was entered into for the purpose of settling the then-pending arbitration proceeding and did not require the performance of any services by Ralph and Charles Abrams, as a partnership or individually.

10. Charles Abrams died on February 22, 1970.

11. The respective estates of the deceased partners continued to operate the partnership business under the name of Ralph and Charles Abrams.

12. On December 12, 1979, the Audit Division issued to the partnership and the estates of the deceased partners a Statement of Audit Changes with regard to the year 1978. The statement proposed unincorporated business tax due in the amount of \$10,165.70, plus interest and penalties pursuant to sections 685(a)(2) and 685(c) of the Tax Law. The proposed changes arose by reason of the partnership's failure to declare and file estimated tax and its failure to pay the balance of unincorporated business tax shown to be due on the 1978 partnership return; and in addition, disallowance by the Audit Division of any deduction for services rendered by partners and the investment tax credits claimed by the partnership. On October 15, 1980, the Audit Division withdrew the proposed changes but offered no explanation for the withdrawal.

13. All partnership returns for the years at issue were prepared on the partnership's behalf by Murray H. Gershon, a certified public accountant and member of the New York bar.

CONCLUSIONS OF LAW

A. That, in general, Tax Law section 683, subdivision (a) (made applicable to Article 23 by section 722) prescribes a three-year period of limitation within which an unincorporated business tax deficiency may be imposed; this period is inapplicable, however, where no return is filed. Section 683(c)(1)(A). The returns filed by the partnership Ralph and Charles Abrams for the years 1969 through 1974 fully disclosed the nature and amount of the various types of income the partnership derived from its real estate activities and sufficiently detailed the nature of the partnership's activities so as to commence the running of the period of limitation. Matter of Arbesfeld, Goldstein v. State Tax Comm., 62 A.D.2d 627. In fact, the Audit Division issued the notices of deficiency without making any inquiries of the taxpayer nor gathering any additional information. Consequently, the deficiencies for the years 1969 through 1974 are cancelled as untimely rendered.

B. That rental income from properties wholly owned by the partnership was exempt from unincorporated business tax by virtue of section 703, subdivision (e), which reads, "An owner of real property, a lessee or a fiduciary shall not be deemed engaged in an unincorporated business solely by reason of holding, leasing or managing real property." On the contrary, rental income from properties owned by other partnerships or corporations in which the partnership Ralph and Charles Abrams was a member or shareholder is not exempted by the above-quoted language. Matter of Elkind v. State Tax Comm., 63 A.D.2d 789 (3d Dept.). Similar reasoning applies with respect to the fees received as building agent under the agreements described in Findings of Fact "5" and "9", even accepting that the partnership and the individual partners never performed any services thereunder.

C. That there exists no basis in the record to allocate the expenses the partnership claimed between its exempt and non-exempt income; consequently, the expenses must be allocated to the exempt income.

D. That there is no evidence in the record from which it can be determined what proportion of the interest and dividends earned by the partnership was used to advance its exempt activities; consequently, the entire amount of interest and dividends must be attributed to the non-exempt activities and held subject to tax.


E. That all penalties and interest in excess of the minimum amount of interest prescribed by statute are remitted.

F. That the petition of the Estate of Ralph Abrams and the Estate of Charles Abrams is granted to the extent indicated in Conclusions of Law "A", "B" and "E"; the deficiencies issued for the years 1969 through 1974 are cancelled in full; and the Audit Division is hereby directed to recompute the deficiencies for 1975 and 1976 in accordance with our decision.

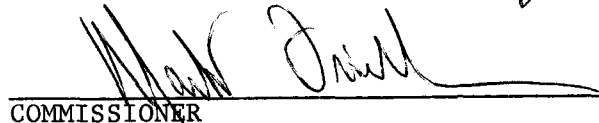
DATED: Albany, New York

STATE TAX COMMISSION

MAY 29 1985


PRESIDENT


COMMISSIONER


COMMISSIONER