STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
DIAN WOODNER	:	ORDER DTA NO. 827879
for Redetermination of a Deficiency or for Refund of New York State and New York City Personal Income Tax under Article 22 of the Tax Law and the Administrative Code of the City of New York for the Year 2009.	:	

Petitioner, Dian Woodner, filed a petition for redetermination of a deficiency or for refund of New York State and New York City personal income tax under article 22 of the Tax Law and the Administrative Code of the City of New York for the year 2009.

Petitioner, appearing by Katten Muchin Rosenman LLP (Michael M. Rosensaft, Esq., of counsel), issued a demand for a bill of particulars, dated September 18, 2017. The Division of Taxation, appearing by Amanda Hiller, Esq. (Charles Fishbaum, Esq., of counsel), brought a motion, dated September 27, 2017, seeking an order pursuant to 20 NYCRR 3000.6 (a) (2), vacating the demand for a bill of particulars. In opposition to the motion, petitioner filed a response to the Division's motion, dated October 25, 2017, and annexed exhibits, which date began the 90-day period for issuance of this order. Based upon the pleadings, motion papers and other documents filed by the parties, James P. Connolly, Administrative Law Judge, renders the following order.

ISSUE

Whether petitioner's demand for a bill of particulars should be vacated.

FINDINGS OF FACT

1. Petitioner, Dian Woodner, commenced this proceeding by filing a petition on October 6, 2016, with the Division of Tax Appeals in protest of a notice of deficiency, dated March 7, 2014, which asserted additional New York State and City personal income tax due, plus interest, for the year 2009.

2. The basis for the asserted deficiency is the audit determination of the Division of Taxation (Division) that petitioner, on her 2009 New York State and New York City personal income tax return, failed to properly report a gain from a transaction in 2009 (2009 Transaction), the background for which is explained below.

3. In 2007, Petitioner owned a 50% membership interest in a limited liability company known as Avenue All Stars LLC (AAS), in which petitioner's sister, Andrea Woodner, owned a 35% membership interest, and the Estate of Jonathan Woodner owned a 15% membership interest. On or about March 30, 2007, AAS formed a limited liability company known as 21 East 67th Street Associates LLC (ESA), in which it was the sole member.

4. On or about July 12, 2007, Petitioner transferred $14,388,000.00 to AAS, which subsequently transferred $14,228,000.00 to ESA. AAS (via ESA) thereafter completed its purchase of real property located at 21 East 67th Street, New York, New York, by transferring the same amount to an attorney escrow account.

5. On or about April 15, 2009, the members of ASA entered into a redemption agreement (Redemption Agreement). Pursuant to that agreement, petitioner transferred her 50% membership interest in AAS in return for AAS's transfer to her of its interest in ESA (the Exchange).

6. The Division filed its answer to the petition on December 15, 2016, and filed an amended answer on or about December 27, 2016. With the permission of the Division of Tax Appeals, the Division filed a second amended answer on August 22, 2017.

7. The second amended answer "[a]ffirmatively states" that the Exchange was "a disguised sale of petitioner's 50% interest in [AAS]" (paragraph 15) and "a taxable event and not a tax-free distribution of property" (paragraph 16).

8. The second amended answer also "[a]ffirmatively states" that the transactions described above:

(a) "cannot be respected under substance over form principles" (paragraph 18);

(b) "constitute a violation of the step transaction doctrine" (paragraph 19);

(c) "were not undertaken for a substantial business purpose" (paragraph 20);

(d) "lacked sufficient economic substance and cannot be respected for tax purposes" (paragraph 21).

9. Paragraphs 22 and 23 of the second amended answer assert that:

"22. . . . [Petitioner] availed herself of [AAS] for transactions, the principal purpose of which was to substantially reduce the present value of [petitioner's] aggregate Federal tax liability in a manner inconsistent with the intent of Subchapter K of the Internal Revenue Code."

23. . . . [Petitioner] violated the anti-abuse rule of Subchapter K of the Internal Revenue Code."

10. Petitioner filed a reply to the second amended answer on September 18, 2017, and on the same day served on the Division a demand for a bill of particulars (Demand), which makes the following demands:

"1. What is the basis for the statement in paragraph 15 of your Second Amended Answer to the Petition of Dian Woodner that 'the Exchange was a disguised sale of Petitioner's 50% membership interest in [AAS]?' In particular, identify: (a) what was sold; (b) when it was sold; (c) by whom it was sold; (d) what the

consideration was; (e) by whom it was bought; and (f) the way in which it was disguised.

2. What is the basis that leads you to believe that [AAS] had the intent or plan to redeem Petitioner's interest in AAS in 2009 when Petitioner made a capital contribution in 2007?

3. What is the basis for the statement in paragraph 16 of the Second Amended Answer that the redemption was 'not a tax-free distribution of property' in light of Section 731 (a)(l) of the Internal Revenue Code of 1986, as amended.

4. What are the bases for the statements in paragraphs 18 and 19 of the Second Amended Answer that the Transaction 'cannot be respected under substance over form principles' and 'constitute a violation of the step transaction doctrine'?

5. What are the bases for the statement in paragraphs 20 and 21 that the 'transactions by Petitioner were not undertaken for a substantial business purpose' and that they 'lacked sufficient economic substance and cannot be respected for tax purposes'?

6. What are the bases for the statements in paragraphs 22 and 23 that Petitioner's 'principal purpose...was to substantially reduce the present value of Petitioner's aggregate Federal tax liability' and that Petitioner 'violated the anti-abuse rule of Subchapter K'?

7. Specifically what taxes was Petitioner seeking to avoid, including the amount and calculation of such taxes and the year(s) in which such taxes would otherwise have been due."

11. On September 27, 2017, the Division filed the instant motion for an order vacating the Demand. The Division's motion argues that the Demand is improper because, first, the Division does not have the burden of proof in this matter and, second, the Demand seeks to discover facts and evidence, rather than crystallize the claims in the second amended answer.

12. In opposition to the Division's motion, petitioner argues that the Demand is necessary because of the vagueness of the Division's pleading, which makes it difficult for petitioner to prepare for hearing, and that the Demand seeks clarification of the Division's second amended answer, and not evidence, as the Division claims.

CONCLUSIONS OF LAW

A. The Tax Appeals Tribunal Rules of Practice and Procedure (Rules) permit the use of a bill of particulars in proceedings in the Division of Tax Appeals "to prevent surprise at the hearing and to limit the scope of the proof" (20 NYCRR 3000.22 [e]).

B. An administrative law judge may be guided but not bound by the provisions of the New York Civil Practice Law and Rules (CPLR) (***see*** 20 NYCRR 3000.5 [a]). Since a wealth of case law has been created under CPLR 3041,"Bill of Particulars in Any Case," it is helpful to refer to that section for guidance in matters before the Division of Tax Appeals.

C. The purpose of a demand for a bill of particulars is to enable the party demanding the particulars to know definitively the claims to be defended against (***see Johnson, Drake and Piper v State of New York***, 43 Misc 2d 513, 515 [Ct of Claims 1964]) or to crystallize the issues that will be raised at hearing (***see e.g. Bassett v Bando Sangsa Co., Ltd.***, 94 AD2d 358, 359 [1st Dept 1983], ***appeal dismissed*** 60 NY2d 962 [1983]). However, a demand for a bill of particulars may not be used to probe into an adversary's legal interpretations or to obtain disclosure of evidence. While drawing a line between a demand for a bill of particulars that seeks evidence versus one that seeks only to crystallize the issues is an inherently difficult task (***see*** Practice Commentary, CPLR 3041, C3041:2 [Bills of Particular, Defined]), it is especially important to make that distinction in this forum, where an Administrative Law Judge may not entertain a motion for discovery (***see*** 20 NYCRR 3000.5 [a]).

D. Generally, under the CPLR, a party need particularize only those matters upon which it has the burden of proof (***see Holland v St. Paul Fire & Marine Ins. Co.***, 101 AD2d 625 [3d Dept 1984).

E. In proceedings in the Division of Tax Appeals a presumption of correctness attaches to a notice of deficiency and the petitioner bears the burden of overcoming that presumption (***see e.g***. ***Matter of Estate of Gucci***, Tax Appeals Tribunal, July 10, 1997, citing ***Matter of Atlantic & Hudson***, Tax Appeals Tribunal, January 30, 1992). Moreover, in cases involving personal income tax, such as here, the burden of proof is upon petitioner, with some exceptions (***see*** Tax Law § 689 [e]). Petitioner acknowledges the general rule that a taxpayer challenging a notice of deficiency issued pursuant to article 22 of the Tax Law has the burden of proof in Division of Tax Appeals proceedings, but argues that the rule should be set aside here because there would be no dispute that petitioner correctly paid her taxes, were it not for the Division's "affirmatively-pled 'disguised sale' and other theories here that petitioner is still struggling to understand." Tax Law § 689 (e) lists four exceptions to its rule allocating the burden of proof to petitioner in Division of Tax Appeals proceedings under article 22 of the Tax Law:

> "(1) whether the petitioner has been guilty of fraud with intent to evade tax;
>
> (2) whether the petitioner is liable as the transferee of property of a taxpayer, but not to show that the taxpayer was liable for the tax;
>
> (3) whether the petitioner is liable for any increase in a deficiency where such increase is asserted initially after the mailing of a notice of deficiency and a petition filed . . .; and
>
> (4) whether any person is liable for a penalty under [Tax Law § 685 (q) or (r)]"

(***see also*** New York City Administrative Code § 11-1789 [e]). Petitioner's argument does not satisfy any of those exceptions and is therefore rejected.

Petitioner next argues that the "disguised sale" allegation in paragraph 16 of the second amended answer comes within the exception in Tax Law § 689 (e) for the issue "whether the petitioner has been guilty of fraud with intent to evade tax" and that therefore the Division has

the burden of proof on that issue. However, petitioner cites no authority in support of its assertion that a "disguised sale" claim is tantamount to a claim of fraud. Moreover, there are reported cases where the taxing authority has prevailed using a "disguised sale" rationale and yet no fraud penalties were imposed (s***ee e.g. SWF Real Estate LLC v Commr.***, 109 T.C.M. 1327 [T.C. 2015]; ***Canal Corp. v Commr.***, 135 T.C. 199 [2010]). Accordingly, it is concluded that the Division's "disguised sale" claim is not tantamount to a claim that petitioner committed fraud here for purposes of Tax Law § 689 (e) (1) and that the Division does not have the burden of proof with regard to that issue or any of the claims in its second amended answer.

F. The rule that a party should not have to particularize any claim on which it does not have the burden of proof is not an invariable one. An exception to this rule is warranted where necessary to further the purpose of the Division of Tax Appeals, which is to provide the public with "a just system of resolving controversies with [the Division] and to ensure that the elements of due process are present with regard to such resolution of controversies" (Tax Law § 2000) . To provide the parties with a fair and orderly system for resolving disputes, the Tax Appeals Tribunal has promulgated the Rules (20 NYCRR 3000.0), which require both parties to file pleadings that give "fair notice of the matters in controversy and the basis for the parties' respective positions" (20 NYCRR 3000.4). Therefore, to the extent that the Division's second amended answer is so vague as to make it difficult for petitioner to prepare for hearing in this matter, the Division may be required to particularize its pleading.

G. The Division's second amended answer, with one exception, invokes specific legal doctrines in defense of the issuance of the notice of deficiency at issue here, such as the anti-abuse rules of Treas. Reg. (26 CFR) § 1.701.2, and the economic substance and substance over form doctrines. Having been apprised of the doctrines that the Division plans on invoking,

petitioner will be able to mount a defense against the notice of deficiency at hearing. Therefore, due process and the Rules do not require the Division to further particularize these paragraphs in the second amended answer. The exception is the allegation in paragraph 16 of the second amended answer that "the Exchange was a taxable event and not a tax-free distribution of property." Because it is unclear what other doctrines this "catch-all" allegation is meant to invoke beyond the doctrines referenced elsewhere in the pleading, the Division is directed to particularize this allegation as requested by paragraph 3 of petitioner's Demand.

H. Accordingly, the Division is directed to supply a bill of particulars in regard to paragraph 3 of petitioner's demand for a bill of particulars within 20 days of the date of this order but, otherwise, the Division's motion to vacate petitioner's demand for a bill of particulars is granted.

DATED: Albany, New York
January 11, 2018

/s/ James P. Connolly
ADMINISTRATIVE LAW JUDGE