STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
JOHN A. AND DEBORAH D. LAURINO	:	DECISION DTA No. 807912
for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Year 1988.	:	

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on September 19, 1991 with respect to the petition of John A. and Deborah D. Laurino, 8 River Lane, Westport, Connecticut 06880. Petitioners appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Paul Lefebvre, Esq., of counsel).

Both parties filed letters in lieu of briefs on exception. The Division of Taxation also filed a reply brief.[1] Petitioners then filed a second letter responding to the Division of Taxation's brief, received November 30, 1992, which began the six-month time period for the Tax Appeals Tribunal to issue this decision. Oral argument was not requested by either party.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUE

Whether the lump sum payment received by petitioner John A. Laurino, a nonresident employed by a New York employer, constituted New York source income subject to personal income tax.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "8" which has been modified. The Administrative Law Judge's findings of fact and the modified finding of fact are set forth below.

[1]Petitioners made a motion to strike the reply brief filed by the Division of Taxation. This motion was denied (Matter of Laurino, Tax Appeals Tribunal, November 5, 1992).

On January 5, 1990, the Division of Taxation issued to petitioners, John A. and Deborah D. Laurino, a Notice of Deficiency asserting personal income tax for the year 1988 in the amount of $1,835.63, plus interest. The Notice of Deficiency also indicated a credit in the amount of $69.73. The notice was issued as a result of an audit of petitioners' personal income tax return for 1988.

The Statement of Personal Income Tax Audit Changes, dated November 24, 1989, indicated the following adjustments to petitioners' personal income tax:

"Based on the information furnished your allocation of wages is as follows:

Total Days		36
Sundays	5	
Saturdays	5	
Holidays	1	
Total Nonworking Days		11
Total Working Days		25
Days worked outside NYS		3
Days worked inside NYS		22

22/25 x $45,000.00 = $39,600.00

Since you worked within and without New York State while employed for Bowery Savings Bank, the portion of the termination pay is taxable to New York State.

Years	Total Wages	NY Wages
1987	$ 89,202.00	$ 89,202.00
1988	45,000.00	39,600.00
Total	$134,202.00	$128,802.00

$128,802.00/$134,202.00 x $170,290.00 = $163,438.00"

Petitioners' wage income for 1988 was therefore computed to be $203,038.00.

Petitioners timely filed a joint New York State and City of New York Nonresident and Part-Year Resident Income Tax Return, Form IT-203, for 1988. Attached to the return was a wage and tax statement, Form W-2, issued to John A. Laurino from The Bowery Savings Bank ("The Bowery") for wages in the amount of $215,290.51.

Petitioners allocated the wage income from The Bowery by employing a fraction with the numerator being 22 days worked in New York State and the denominator being 236 total days worked in the year.

On July 13, 1987, petitioner John A. Laurino[2] entered into an employment contract with The Bowery Savings Bank, 110 East 42nd Street, New York, New York 10017. The contract provided, in part, as follows:

(a) Petitioner's title would be Senior Vice President and Marketing Director.

(b) The base salary would be $165,000.00 per annum to be effective on July 20, 1987.

(c) Petitioner's first year annual bonus would be a minimum of $10,000.00 and would be payable in January 1988.

(d) Petitioner was to receive a moving expense allowance, bridge loan financing and a discount on mortgage points when purchasing a new home in the New York metropolitan area and travel and entertainment expenses during his employment.

(e) Petitioner was entitled to a severance payment upon the change of control of The Bowery, provided in the employment contract as follows:

> "During your first two years of employment should there be a change in control of The Bowery and if, within 120 days of such change of control, your employment at your current salary is not extended in writing for at least one year by The Bowery, you would be entitled to receive a severance payment equal to one year's salary. The term 'change of control' means any transaction or series of transactions by virtue of which more than 50% of the voting power of the stock of The Bowery changes hands." (Paragraph 7 of the employment contract).

Prior to accepting the position with The Bowery, Mr. Laurino had similar employment in Philadelphia, Pennsylvania. In addition, he turned down a position with another bank in New York City to accept the offer of The Bowery.

On January 29, 1988, The Bowery was acquired by H. F. Ahmanson & Company, a holding company for Home Savings of America. The company, located in California, was a highly-centralized organization with all senior and executive management positions located at the California offices. All marketing related activities were directed from California, and the chief marketing officer of Home Savings was stationed there. The individual who held this position

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[2]Deborah D. Laurino is a petitioner only by reason of having filed a joint return with John Laurino. Therefore, all references to "petitioner" will be to John Laurino only.

became, after the acquisition of The Bowery and petitioner's resignation, the senior vice president and chief marketing officer of The Bowery as well, and continued to work in California.

During his employment, petitioner was engaged in various marketing projects, some jointly with Home Savings of America. The projects included a 1988 marketing plan, a study involving The Bowery's entry into the insurance and investment product businesses, a public relations plan and a communications plan concerning the merger of The Bowery with Home Savings from a marketing perspective. Several of these projects were implemented after petitioner's resignation.

On January 27, 1988, The Bowery paid to petitioner a bonus of $10,000.00 pursuant to the agreement of employment dated July 13, 1987. Petitioner also received, in 1988, deferred compensation from 1987 of $18,500.00 and salary in the amount of $16,500.00. Petitioners concede that the total of this compensation ($45,000.00) is subject to the imposition of New York State personal income tax.

We modify finding of fact "8" of the Administrative Law Judge's determination to read as follows:

> Petitioner and The Bowery entered into an employment termination agreement on February 4, 1988. The agreement was a direct result of the change of control of The Bowery on January 29, 1988 and related management changes. Pursuant to the agreement, The Bowery and petitioner agreed to the following:
>
> (a) The Bowery paid to petitioner $165,000.00 in full satisfaction and discharge of The Bowery's obligations arising out of or in connection with petitioner's employment, its termination, the change in control of The Bowery and under the terms of the letter dated July 13, 1987 between The Bowery and petitioner relating to his employment.
>
> (b) The Bowery transferred and delivered ownership of the following equipment to petitioner:
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> Apple MacIntosh SE Personal Computer
> Image Writer Printer
> Keyboard
> "Mouse"
> Carrying case for personal computer equipment
> Personal computer software consisting of "X-Cel", "Project" and "MacWrite".

> The estimated fair market value of the personal computer equipment and software transferred was $3,322.00.
>
> (c) Petitioner was to be reimbursed for long-distance telephone calls made during the period February 4, 1988 (his last day of employment) to April 30, 1988 for the purpose of seeking employment.
>
> (d) In consideration of the above, petitioner released The Bowery, its parents, subsidiaries and affiliates from any claim he might have had, arising out of or in connection with his employment, the change in control of The Bowery that occurred January 29, 1988, or for any payments or other obligations of The Bowery due under the employment agreement (letter of July 13, 1987). The payments were not conditioned upon any future services being rendered by petitioner, and,in fact, no services were thereafter rendered.[3]

During the year at issue, petitioners were residents of the State of Connecticut.

OPINION

In the determination below, the Administrative Law Judge held that the income received by petitioner as a result of a termination agreement was not New York source income within the meaning of Tax Law § 631(b)(1)(B), as the focus of the termination agreement was petitioner's future status, not his past services (citing Matter of Donahue v. Chu, 104 AD2d 523, 479 NYS2d 889). In reaching this conclusion, the Administrative Law Judge found the following to be significant: 1) the object of the termination agreement was to put petitioner in approximately the same position in which he would have been had he remained employed by the Bowery; 2) the payments under the termination agreement did not arise out of petitioner's past services, as evidenced by petitioner's receipt of his salary, bonus and deferred compensation payment in the short period of time petitioner was employed during 1988; and 3) any future employment rights possessed by petitioner would have been exercised in California, not New York State. It was also concluded that paragraph 7 of the termination agreement does not support the Division of Taxation's (hereinafter the "Division") position because petitioner's right to a lump sum payment under this paragraph would be based on petitioner's future employment status with the Bowery, not on services rendered in the past (see, Determination, p. 10).

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[3]In paragraph (d) the date July 13, 1977 was changed to July 13, 1987 to accurately reflect the record.

The Administrative Law Judge also held that the the $45,000.00 income which petitioner conceded was subject to tax by New York State was properly allocated based on the number of days worked within and without New York State in accordance with 20 NYCRR 131.18(b).

On exception, the Division asserts that Matter of Donahue v. Chu (supra) is distinguishable from the facts of this case. The Division contends that in Donahue, "the petitioner and his employer negotiated a settlement which abrogated the initial employment contract and, in effect, 'bought out' the petitioner's remaining term of employment. The money received by the petitioner was clearly a payment of future services from which the employer wished to be released" (Division's letter brief, p. 1). The Division contends that in the present case the payment was made in accordance with the initial employment contract which was, in effect, a guaranteed minimum offered to petitioner as an inducement to relocate and take employment with a bank the future of which was uncertain.

The Division also attempts to distinguish Donahue based on the intentions of the contracting parties in these two cases. Specifically, the Division states that unlike in Donahue, where the parties were contracting in contemplation of termination, the parties in the present case were negotiating at the beginning of petitioner's employment and because this payment provision covered only the first two years of employment, the payment was not intended for future services.

The Division also argues that because petitioner secured this benefit upon entering into his employment contract and earned the right to receive it by going to work for the Bowery, the income is taxable to New York (citing Matter of Halloran, Tax Appeals Tribunal, August 2, 1990). Finally, the Division asserts that because petitioner's employment agreement characterizes the payment at issue as "severance pay," and the former State Tax Commission consistently held that severance pay was connected to prior services rendered, the income is taxable by New York State.

In response, petitioner argues that this case must be viewed apart from cases where "the taxpayers involved were officially kept on their previous New York state employers' payrolls"

(Petitioner's letter brief, p. 1). Petitioner claims that the facts of this case instead parallel those in Matter of Donahue v. Chu (supra) because "there was no post-merger employment continuation" and "had there been . . . it would have taken place outside New York State" (Petitioner's letter brief, p. 1). Petitioner also argues that because he secured a post-merger right to employment by virtue of his employment agreement and the Bowery's personnel policy, and that additional value was offered by H.F. Ahmanson as an incentive to petitioner to surrender all future rights, the payment at issue should be viewed, as in Donahue, as a "buyout."

We reverse the determination of the Administrative Law Judge.

Tax Law § 631(a) defines the New York source income of a nonresident individual. This section provides:

> "General. The New York source income of a nonresident individual shall be the sum of the 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 . . ." (Tax Law § 631[a], emphasis added).

Income which is "derived from or connected with New York sources" shall be attributable to . . . a business, trade, profession, or occupation carried on in this state . . ." (Tax Law § 631[b][1][B]).

Both parties have cited Matter of Donahue v. Chu (supra) as the primary authority for their respective positions. The relevant facts in Donahue are as follows: the taxpayer, a resident of Connecticut, entered into a five-year employment contract with his New York employer. The agreement provided that at the conclusion of the five-year period, the taxpayer would provide consulting services over the next ten years at a rate of $20,000.00 per year. In the fifth year of the contract, the taxpayer and the corporation entered into a second agreement terminating the initial employment agreement. As consideration for the relinquishment of these future rights, the taxpayer received the remainder of his final year's salary, as well as the sum of $107,361.00.

In Donahue, the employment contract provided the petitioner with an annual salary, benefits, and the right to $20,000.00 annually for ten years in exchange for his promise to

provide services as an employee and later as a consultant.[4] Therefore, at the moment petitioner entered into the contract, he had secured a right to future employment. In the later agreement, which terminated the employment contract, the petitioner received a payment in exchange for relinquishing these rights. Because these rights to future employment were originally secured by consideration having no connection with New York (i.e., the promise to work in the future), the Appellate Division held that this payment was not New York source income. Thus, we read Donahue to stand for the proposition that where a nonresident possesses a right to future employment secured by consideration having no connection with New York, and relinquishes that right in exchange for a lump sum settlement, the lump sum settlement is not taxable to New York.[5]

Petitioner contends that because the lump sum payment was intended to compensate him for work that he would have performed in the future, and that such work would have been performed in California, this income should not be taxable in New York. We disagree. Instead, we conclude that in determining whether income is "derived from or connected with New York sources" it is necessary to identify the activity upon which the income was secured or earned (Matter of Halloran, supra). Thus, in making this determination, the consideration given by petitioner in exchange for the right to the income at issue is the controlling factor.

PETITIONER'S EMPLOYMENT CONTRACT WITH BOWERY

The written agreement dated July 13, 1987 between petitioner and Bowery sets forth the terms of petitioner's employment, including salary, bonus, moving expenses, and other benefits

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[4]See, Matter of Donahue (State Tax Commn., May 27, 1983) (finding of fact "4"). See also, Weiner v. McGraw-Hill, Inc. (57 NY2d 458, 457 NYS2d 193, 196 [existence of right to employment does not necessitate a reciprocal obligation by employee to continue working when other consideration is received by employer]).

[5]Further support for this reading is found in 20 NYCRR former 131.5 which states in relevant part: "[i]tems of income . . . attributable to intangible personal property of a nonresident individual . . . do not constitute items of income . . . derived from or connected with New York State sources . . ." (see, McKinney's Cons Laws of NY, UCC § 9-106, Official Comment [Contract rights included within the definition of "general intangibles"]; cf., Matter of Walsh, Tax Appeals Tribunal, November 19, 1992 [held that income received by a nonresident taxpayer in accordance with a contract where the consideration for the income was the taxpayer's past services in New York is New York source income (citing 20 NYCRR former 131.4[d])]).

to be received by petitioner upon his joining the Bowery as Senior Vice President and Marketing Director. Paragraph 7 of this agreement, which is the focus of this dispute, states in relevant part:

> "[d]uring the first two years of employment should there be a change in control of the Bowery and if, within 120 days of such change of control, your employment at your current salary is not extended in writing for at least one year by the Bowery, you would be entitled to receive a severance payment equal to one year's salary . . ." (emphasis added).

Petitioner makes the following two-pronged argument in regard to his employment contract: 1) that this employment contract "expressly provided for post-merger rights in the form of employment" and 2) that "[t]he lump sum payment was an alternative to the continuation of those future rights" (Petitioner's letter brief, p. 1). We will address the first prong of this argument first.

EMPLOYMENT AT WILL

Although petitioner's entitlement to one of these two conditional rights (a lump sum payment or the right to future employment) under paragraph 7 was conditioned upon a change of control within "the first two years of [petitioner's] employment," this term did not bestow upon petitioner a right to employment for two years, or any future period. The law in New York is clear that "absent a constitutionally impermissible purpose, a statutory proscription, or an express limitation in the individual contract of employment, an employer's right at any time to terminate an employee at will remains unimpaired" (Murphy v. American Home Prods. Corp., 58 NY2d 293, 461 NYS2d 232, 237, emphasis added). "Where an employment is for an indefinite term it is presumed to be a hiring at will which may be freely terminated by either party at any time for any reason or even for no reason" (Murphy v. American Home Prods. Corp., supra, 461 NYS2d 232, 235, citing Martin v. New York Life Ins. Co., 148 NY 117). In our view, this two-year period was merely intended to establish the period within which these conditional rights granted to petitioner would either vest and/or fail. In addition, we note that this "two year" reference does not give rise to an implied obligation of good faith and fair dealing which would prohibit the Bowery from terminating petitioner, as these principles are not recognized in an employment at will (Murphy v. American Home Prods. Corp., supra; Ingle v. Glamore Motor Sales, 73 NY2d

183, 538 NYS2d 771, 773). Because there is no language contained in the contract which suggests a definite term of employment, we conclude that the parties failed explicitly to reverse the presumption of employment at will required under New York law (Murphy v. American Home Prods. Corp., supra).

In light of our conclusion above, any attempt to align this employment agreement with that in Donahue, where a right to future employment was secured by the petitioner's mere promise to work in the future (a detriment unconnected with New York), misconstrues the terms of the agreement. Under this agreement, petitioner's employment with the Bowery could have been terminated prior to a "change of control" "for any reason or even for no reason," with the conditional rights under the agreement terminated along with it. In our view, what the Bowery sought from petitioner in exchange for the right to future employment or a lump sum payment was petitioner's act of continued service to the Bowery up to the time that a change of control occurred. Thus, unlike Donahue, petitioner's entitlement to a "future" right was to be secured by an act, not a mere promise. Because it was this continuing service to the Bowery performed by petitioner predominantly in New York which constituted the consideration for the lump sum payment, we hold that the proper percentage[6] of this payment was taxed by New York, as it was "derived from or connected with New York sources" (Tax Law § 631; Matter of Halloran, supra; see, Matter of Walsh, supra; cf., Donahue v. Chu, supra).

The second prong of petitioner's argument, that the lump sum payment was an alternative to future employment which would have occurred outside New York and was, thus, not taxable to New York, is also without merit.

In analyzing these conditional rights contained in the contract, petitioner attempts to exalt the right to future employment as the only true right,[7] with the lump sum merely serving as

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[6]See, finding of fact "2" for days worked by petitioner within and without New York.

[7]In order to justify this position, petitioner must argue that the Bowery's failure to extend petitioner's employment was a breach of a promise to do so, with the lump sum payment representing a form of liquidated damages. We fail to read such a promise into this agreement. Under the employment agreement, upon the Bowery undergoing a "change of control," the Bowery had an option, exercisable within 120 days, to fulfill its obligation in one of two ways: Make a lump sum payment to petitioner or extend his employment contract for one year. Because the

payment for this employment right, which would have been exercised outside New York. In taking this position, petitioner ignores a key distinction between these two benefits. The future employment required an additional detriment from petitioner -- the act of working in the future -- before a taxable event (the receipt of income) for this future work would arise. In contrast, petitioner's right to the lump sum payment was complete at the time the February 4, 1988 agreement was signed and was earned by his past services. Thus, we find the premise of petitioner's argument, i.e., that potential future employment and the definite lump sum payment are indistinguishable for tax purposes, is flawed.

BOWERY'S PERSONNEL POLICIES

Petitioner also claims that "the Bowery had [a] personnel policy in place that protected all employees from arbitrary dismissal" (Petitioner's letter brief, p. 1). It has been held in New York that, "on an appropriate evidentiary showing, a limitation on the employer's right to terminate an employment of indefinite duration might be imported from an express provision therefor found in the employer's handbook on personnel policies and procedures" (Murphy v. American Home Prods Corp., supra, 461 NYS2d 232, 237, citing Weiner v. McGraw-Hill, Inc., supra). The sole piece of documentary evidence[8] submitted by petitioner on this point is a page, dated "2/88," from the Human Resources Policy and Procedure Manual of H.F. Ahmanson & Company titled "Equal Employment Opportunity Policy" (Exhibit "4"). Because this document has no apparent bearing on the termination policy of the Bowery prior to the merger, we hold that petitioner has failed to establish a continued right to employment on this basis.

Bowery chose the former option, a right to future employment never arose.

[8]At the close of the hearing on March 26, 1991, the Administrative Law Judge, in preparing to close the record, asked the parties if they desired to submit any additional evidence. They stated that they did not. The Administrative Law Judge informed the parties that he would not accept any further evidence upon closing the record, and proceeded to close the record. Petitioner subsequently submitted a letter dated April 19, 1991 describing the Bowery's termination policy as explained to him by the Bowery's general counsel. Despite his clear instructions at the close of the hearing, the Administrative Law Judge admitted this letter into evidence on April 22, 1991. We hold that this was an error. In keeping with our policy of maintaining a hearing process which is both defined and final, we conclude that this letter was improperly admitted into evidence (Matter of Schoonover, Tax Appeals Tribunal, August 15, 1991; Matter of A & J Auto Repair Corp., Tax Appeals Tribunal, May 6, 1993). Thus, we did not consider petitioner's letter of April 19, 1991 in rendering our decision.

Finally, petitioner contends that, contrary to the Division's assertions, the actions taken were "not expressly contemplated by the parties to the contract," and "the [lump sum] payment was only part of the total settlement" received by petitioner (Petitioner's letter brief, p. 2). We fail to see the merit in this argument. The termination agreement of February 4, 1988 clearly states that:

> "[t]he payment of $165,000 is being paid to and is accepted by you in full satisfaction and discharge of The Bowery's obligations to you arising out of your employment, its termination, the change of control of the Bowery and under the terms of [the agreement] relating to your employment."

It is true that petitioner received other benefits under this termination agreement. However, this does not magically sever the connection between petitioner's right to this income and his acts performed in New York to secure this right. As stated in the termination agreement, the lump sum payment satisfied the obligation arising out of the employment agreement. Petitioner's receipt of additional benefits does not alter this fact.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is granted;

2. The determination of the Administrative Law Judge is reversed;

3. The petition of John A. and Deborah D. Laurinois denied; and

4. The Notice of Deficiency dated January 5, 1990 is sustained.

DATED: Troy, New York
May 20, 1993

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner

/s/Maria T. Jones
Maria T. Jones
Commissioner