STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
BRUCE M. AND CLAIRE M. MONTGOMERIE	:	DECISION DTA NO. 812425
for Redetermination of a Deficiency or for Refund of New York State and City Personal Income Taxes under Article 22 of the Tax Law and the New York City Administrative Code for the Year 1986.	:	

Petitioners Bruce M. and Claire M. Montgomerie, 17 Windabout Drive, Greenwich, Connecticut 06831, filed an exception to the determination of the Administrative Law Judge issued on October 28, 1999. Petitioners appeared by Willkie, Farr & Gallagher (Patrick J. Carmody, Esq., of counsel). The Division of Taxation appeared by Barbara G. Billet, Esq. (Michael J. Glannon, Esq., of counsel).

Petitioners filed a brief in support of their exception. The Division of Taxation filed a brief in opposition and petitioners filed a reply brief. Oral argument was not requested.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUE

Whether the Division of Taxation properly required petitioners to prorate their partnership income between a period of time when they were residents of New York State and a period of time when they were nonresidents of New York State.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "8," "9," "10" and "11" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

The Division of Taxation ("Division") issued to petitioners, Bruce M. Montgomerie and Claire M. Montgomerie, a Statement of Audit Changes, dated July 5, 1988, asserting a deficiency of New York State income tax for 1986 in the amount of $18,344.82 plus interest.[1] Petitioner's taxable New York income was recomputed by the Division and the following explanation for the recomputation was provided:

> The limitation percentage must be computed and applied to itemized deductions, exemptions and child care credit on the nonresident return.
>
> When two returns are filed due to change in resident status during the tax year, the distributive share of partnership income or loss must be prorated by months between the resident and nonresident periods. Your return has been corrected and tax recomputed . . . .

By letter dated August 2, 1988, petitioner responded to the Division's statement and protested all of the adjustments made. As pertinent, his letter states:

> 1. The only explanation you give for our proposed adjustment is that when two returns are filed due to change in resident status, the distributive share of partnership income or loss must be pro rated. This is not correct and your statement is contrary to your own Regulation.
>
> Regulation § 148.6, in effect for 1986 and still in effect, explicitly states that a partner's distributive share is *not* pro rated between resident and non-

[1] It appears that the income which is the source of this dispute is that of Mr. Montgomerie, and Mrs. Montgomerie is included as a petitioner here only because she filed a joint return with her husband. Accordingly, all references in this decision to "petitioner" may be understood to mean Bruce M. Montgomerie.

> resident periods. *Such shares are included in the period in which the partnership year ends*. (See copy of Regulation § 148.6 enclosed). (Emphasis added.)
>
> 2. Your N.Y. income, adjustments and additions all vary from mine as reported but you state no reason for this difference. I believe you must explain these changes or allow my reported position to stand, especially since your basic reason for your proposed audit adjustment, as discussed in point 1. above, is wrong.

The Division responded to petitioner in a letter dated in September 1988 (the day of the month is illegible). This letter explains the Division's position as follows:

> The Court of Appeals (*McNulty etal* [sic] *v. The New York State Tax Commission*) recently ruled the following:
>
> When two returns are required to be filed due to a change of residence, and the taxpayer is a member of a partnership or a shareholder of a New York S corporation, any distributive share should be prorated by months, over the entire tax year of the taxpayer.
>
> This change will apply to all tax years where the statute of limitations has not expired.
>
> Your partnership income/(losses), Federal adjustments and New York modifications have been prorated on an 11 month/1 month basis. In the nonresident period New York nonresident partnership income/(loss) were not included as income.
>
> New York State Regulation 148.6 is in the process of being revised.

On or about February 10, 1989, the Division issued a Notice of Deficiency to petitioners asserting a deficiency of income tax for 1986 in the amount of $18,344.82 plus interest. No penalty was imposed.

Following a conciliation conference held on January 10, 1990, the Division issued a Conciliation Order, dated April 6, 1990, reducing the asserted deficiency for 1986 to $11,861.00 but otherwise sustaining the deficiency. No penalty was imposed.

On July 6, 1990, petitioner mailed a petition to the Division of Tax Appeals protesting the Notice of Deficiency. The petition was dismissed by the Division of Tax Appeals on its own order on the ground that it was not filed within 90 days of the mailing of the Conciliation Order. Petitioner then paid the asserted tax deficiency and filed a claim for refund of tax in the amount of $16,321.65.

On December 30, 1991, the Division issued to petitioner a Notice of Disallowance denying the claim for refund of taxes paid for 1986.

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

> Petitioner then filed a verified petition in the Division of Tax Appeals. The petition was signed by Bruce M. Montgomerie and Claire M. Montgomerie.[2]

We modify finding of fact "9" of the Administrative Law Judge's determination to read as follows:

> Petitioners filed their New York State tax return for 1986 on August 8, 1987.[3] They filed a resident return for the period January 1, 1986 to December 1, 1986 and a nonresident return for the period December 1, 1986 through December 31, 1986.[4]

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[2]We modified finding of fact "8" of the Administrative Law Judge's determination by deleting extraneous matters.

[3]The facts as stated in findings of fact "9" and "10" of the determination were taken from the verified petition. Since neither party submitted documentary evidence to establish facts crucial to this determination (e.g., petitioner's 1986 personal income tax return), and they were unable to agree on stipulated facts, the Administrative Law Judge relied upon facts which she deemed admitted from the petition.

[4]We modified finding of fact "9" of the Administrative Law Judge's determination to more accurately reflect the record. Petitioners alleged in their petition that from January 1, 1986 through December 31, 1986, Mr. Montgomerie was a general partner of Willkie, Farr & Gallagher, a New York-based general partnership, and that Willkie, Farr and Gallagher used the calendar year as its taxable year for 1986. The Administrative Law Judge deemed these allegations admitted and included them as part of her finding of fact "9." However, the Division's

(continued...)

We modify finding of fact "10" of the Administrative Law Judge's determination to read as follows:

> Petitioner claims that he reported his New York State partnership income in accordance with former section 148.6 of the Division's regulations, in effect at the time the New York State return was filed. Under the regulation, the distributive share of income received from a partnership was to be reported in the portion of the taxable year in which the taxable year of the partnership ends. The distributive share of income was not to be prorated between the resident and nonresident income tax returns. The Division's regulation 148.6 directed that partnership income received by petitioner be reported on his New York nonresident return.[5]

We modify finding of fact "11" of the Administrative Law Judge's determination to read as follows:

> Petitioner and the Division did not file an executed stipulation of facts, and there was no testimony. Petitioner did not offer a copy of his tax returns for 1986 to show how he computed the tax. Nor did he offer proof to show that during 1986 he was employed by Willkie, Farr & Gallagher, a New York-based general partnership, as claimed. Further, petitioner did not offer proof to show that Willkie, Farr & Gallagher used the calendar year as its taxable year for 1986.[6]

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

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[4](...continued)
Answer "denied knowledge or information sufficient to form a belief" as to these allegations. The "denial of knowledge or information sufficient to form a belief" is deemed a denial under CPLR 3018 and under our rules (20 NYCRR 3000.4[b][2][i]). Matters thus denied are placed in dispute and are subject to petitioner's burden of proof (20 NYCRR 3000.15[d][5]). Therefore, it was error to deem these statements admitted and to include them as a finding of fact in the absence of other proof.

[5]We modified finding of fact "10" of the Administrative Law Judge's determination to more accurately reflect the record. We have deleted that part of the finding which was erroneously based on paragraph XII of the petition, which was denied by the Division's Answer and for which no other proof was offered.

[6]We modified finding of fact "11" of the Administrative Law Judge's determination by deleting extraneous matters and by adding findings germane to the decision.

The law in effect for the 1986 tax year provided that if an individual changed his status during his taxable year from resident to nonresident, or from nonresident to resident, he must file one return as a resident for the portion of the year during which he was a resident, and one return as a nonresident for the portion of the year during which he was a nonresident, subject to such exceptions as the Tax Commission may prescribe by regulation (Tax Law former § 654[a]).[7]

In ***Matter of McNulty v. New York State Tax Commn.*** (70 NY2d 788, 522 NYS2d 103), the taxpayers, whose sole source of income in 1979 was a distributive share of the earnings of a New York partnership, moved their residence from New York to New Jersey in August of 1979. In accordance with former section 654, they filed a resident return for January 1, 1979 through August 1979 and a nonresident return for the period August 1979 through December 31, 1979. Thus far, the Administrative Law Judge noted, the taxpayers in ***McNulty*** and petitioner operated under similar circumstances. However, the ***McNulty*** taxpayers, unlike petitioner, did not comply with the related tax regulation, 20 NYCRR former 148.6, which required that taxpayers who move in or out of the State during the tax year treat partnership gains or losses as having all accrued in the "portion of the taxable year" in which the partnership's own tax year ends. As noted by the Court of Appeals in ***McNulty***, the effect of this regulation was "to compel the taxpayer who has changed residence during the tax year to report all of his partnership income on one or the other of his separate tax returns for that year — regardless of when the income was actually received" (***Matter of McNulty v. New York State Tax Commn.***, ***supra***, 522 NYS2d, at 104).

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[7]Section 654 was repealed by the Legislature effective January 1, 1988.

The Administrative Law Judge pointed out that application of regulation 148.6 in the ***McNulty*** case required the taxpayers to report all of their income on the nonresident tax return and no income on their resident return. This resulted in an increase to McNulty's tax liability because Tax Law § 654(c)(e) required the taxpayers to prorate and allocate their personal exemptions and deductions between their resident and nonresident returns. In effect, the taxpayers were deprived of the beneficial use of the exemptions and deductions reported on the resident return because there was no income against which they could be applied.

The ***McNulty*** Court concluded that regulation 148.6 was an invalid exercise of the Tax Commission's authority because requiring annual partnership distributions to be reported in their entirety on one of the two returns "without regard either to when such distributions are received or to proration. . . is inconsistent with [the] legislative policy [of section 654 of the Tax Law]" (***Matter of McNulty v. New York State Tax Commn.***, ***supra***, 522 NYS2d, at 104). The Administrative Law Judge noted that with respect to the statute's legislative policy, the ***McNulty*** Court stated that section 654:

> evinces a clear legislative intention that most forms of income, as well as exemptions and standard deductions, be allocated between the taxpayer's resident and nonresident returns in a manner *that either reflects the actual date of receipt and expenditure or encompasses an annual amount distributed on a proportionate basis* (***see***, Tax Law § 654 [b], [e], [f]; ***cf.***, § 654 [c], [i] [governing "special accruals" and "lump sum" distributions]) (***Matter of McNulty v. New York State Tax Commn.***, ***supra***, 522 NYS2d, at 104, emphasis added).

This petitioner argues that the ***McNulty*** opinion permitted, but did not mandate, the proration of partnership income and losses.[8] According to petitioner, the ***McNulty*** opinion created a rule of narrow application intended to redress an inequitable result which stemmed from application of regulation 148.6 under the facts of that case. Petitioner asserts that since substantial income was reported on his 1986 resident return, he suffered no loss of the benefit of exemptions and deductions as was the case in ***McNulty***.[9] Based on this purported difference in the facts of the two cases, petitioner claims that application of regulation 148.6 does not lead to an inequitable result and must be permitted.

The Administrative Law Judge pointed out that our decision in ***Matter of Wertheimer*** (Tax Appeals Tribunal, January 12, 1995)[10] *mandates* proration of petitioner's partnership income to the resident and nonresident returns filed for 1986. The Administrative Law Judge noted that we explained our reasoning in ***Wertheimer*** as follows:

> Although a partnership computes its net income, section 701 of the Internal Revenue Code provides that the partners are liable for the tax on the income. Pursuant to section 702 of the Internal Revenue Code, the tax is determined by each partner reporting his distributive share of, inter alia, the partnership's income, gain and losses. Section 706(a) of the Code requires that *each partner's distributive share of the income, gain and loss* be included in that partner's taxable income for the taxable year of the partnership

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[8]This same argument was made in ***Matter of Wertheimer*** (Tax Appeals Tribunal, January 12, 1995).

[9]Since neither party placed petitioner's 1986 personal income tax returns in evidence, and the parties did not execute a stipulation of facts, there is no factual basis in the record to support these arguments.

[10]At the request of petitioner, this matter was held in abeyance pending our decision in the *Matter of Wertheimer* (Tax Appeals Tribunal, January 12, 1995, remanded); ***Matter of Wertheimer*** (Tax Appeals Tribunal, March 14, 1996). "It was understood that the two matters were factually similar and the outcome of Wertheimer would determine the outcome" in this case (Division's Brief, p. 2). After the Tribunal issued the two decisions in Wertheimer, the Montgomeries "decided . . . to proceed before the Division of Tax Appeals raising the same issues which were decided in favor of the Tax Department in the ***Matters of Wertheimer***" (Division's Brief, p. 3). Petitioner in Wertheimer was a partner in the New York legal partnership of Willkie, Farr & Gallagher.

> ending within or with the partner's tax year. *A partner is required to report and pay tax on his distributive share of the net income of the partnership in this manner without regard to whether this amount was actually distributed or distributable to him in that year* (***United States v. Basye***, 410 US 441, ***reh denied*** 411 US 940) (***Matter of Wertheimer***, Tax Appeals Tribunal, January 12, 1995, emphasis added.)

Based on this explanation, the Administrative Law Judge noted, we found that the ***McNulty*** opinion *required* an allocation of partnership income that reflects "either the *actual date of receipt* and expenditure or encompasses an annual amount distributed on a proportionate basis" (***Matter of Wertheimer***, Tax Appeals Tribunal, January 12, 1995, quoting ***Matter of McNulty v. New York State Tax Commn., supra,*** 522 NYS2d 103, 104). The Administrative Law Judge also pointed out that our decision stated that "where a partner's distributive share of income is reported without regard to actual receipt, the only possible method of allocation under section 654 is on a proportionate basis throughout the year" (***Matter of Wertheimer***, Tax Appeals Tribunal, January 12, 1995). This petitioner argues that he reported his distributive share of partnership income without regard to actual receipt, but based on the Internal Revenue Code § 706(a) requirement that such income be included in the partner's taxable income for the taxable year of the partnership ending within or with the partner's tax year — in this case, December 1986.[11] The Administrative Law Judge concluded that the holdings of ***Wertheimer*** and ***McNulty*** require that this income be allocated between the resident and nonresident return on a proportionate basis.

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[11]In a footnote, the Administrative Law Judge notes that petitioner stated in his letter to the Division dated August 2, 1988 that his distributive share of partnership income was reported in keeping with regulation 148.6, which required such shares to be included in the period in which the partnership year ends. The Administrative Law Judge viewed this letter as conceding that the income was not reported when actually received. This letter is not part of the record.

Petitioner also argued that ***Wertheimer*** is distinguishable because that case involved the proper reporting of partnership losses rather than income. The Administrative Law Judge noted the irony here, since the petitioners in ***Wertheimer*** argued that the holding in ***McNulty*** applied only to allocation of partnership income and not to losses. The Administrative Law Judge concluded that our decision in ***Wertheimer*** held that the ***McNulty*** opinion created a general rule applicable to both partnership income and losses.

Like petitioner here, the Wertheimers argued that the decision in ***McNulty*** could not be applied retroactively to them.[12] After deciding the primary issue raised by the parties in ***Matter of Wertheimer*** (Tax Appeals Tribunal, January 12, 1995), we remanded the case for a determination by the Administrative Law Judge on the question of whether the ***McNulty*** decision should be given retroactive application to the income tax return filed by the petitioners for 1986 (the same year at issue here). Following the Administrative Law Judge's determination on remand, we affirmed, holding that the construction of Tax Law § 654 by the Court of Appeals in ***McNulty*** must be applied retroactively to the petitioners' 1986 tax return (***see***, ***Matter of Wertheimer***, Tax Appeals Tribunal, March 14, 1996). We rejected the argument that retroactive application was unfair because petitioners had relied on an established regulation which was in effect at the time they filed their return, and stated:

> It is undisputed that the application of ***McNulty*** will require petitioners to pay more tax for 1986 than they reported on their return; however, it is not obvious to us that a taxpayer has a substantial equitable right to pay less tax than a rule announced by the Court of Appeals would require. Petitioners would have a

[12]The Court of Appeals decision in ***Matter of McNulty v. New York State Tax Commn***. (***supra***) was published on the same day as Wertheimer's tax returns were in-date stamped as received by the Division for tax year ending 1986.

> stronger equitable argument if they could identify specific actions they took in reliance on rule 148.6 which now work to their detriment under the retroactive application of ***McNulty*** [footnote omitted]. Petitioners' claim that they relied on the regulation when they filed their return would be pertinent if the Division had assessed penalty. However, the Division did not assert penalty and without penalty we do not see that petitioners were prejudiced by their reliance on the regulation. Thus, we see little weight to the equitable burden imposed on petitioners by the retroactive application of ***McNulty*** (***Matter of Wertheimer***, Tax Appeals Tribunal, March 14, 1996).[13]

From this, the Administrative Law Judge concluded that our holding in ***Wertheimer*** requires the application of the ***McNulty*** decision to petitioner's 1986 tax year and rejection of his argument that such an application is inequitable.

ARGUMENTS ON EXCEPTION

Petitioner on exception makes the same arguments as he did below. These arguments were, with one exception, also made in ***Matters of Wertheimer*** (Tax Appeals Tribunal, January 12, 1995 and March 14, 1996). The arguments are as follows.

Petitioner filed his New York resident and nonresident personal income tax returns for tax year 1986 on August 8, 1987. The Court of Appeals handed down its decision in ***McNulty*** on October 15, 1987. Petitioner argues that: 1) The decision in ***McNulty*** should not be applied retroactively to them, because he filed his tax returns more than two months before that decision was issued and fully in accordance with Division regulation 148.6 then in effect; 2) His returns as filed are consistent with ***McNulty*** because that case permitted, but did not mandate, proration of partnership income; 3) Our decision in ***Wertheimer*** is inapplicable to petitioner, because that case dealt with partnership losses, not partnership income; and 4) It would be unfair and

[13]It is noted that no penalties were imposed upon this petitioner either.

inequitable to apply the decision in ***McNulty*** to petitioner, because he could not foresee that the law would change.

OPINION

With the exception of the fact that ***Wertheimer*** dealt with partnership losses and this case purportedly deals with partnership income, the two cases are identical. Each of the arguments here have already been raised and decided in ***Matter of McNulty*** (***supra***) and ***Matters of Wertheimer*** (January 12, 1995 and March 14, 1996). One difference between the earlier cases and the instant matter, however, is that in ***McNulty*** and ***Wertheimer,*** the petitioners put evidence in the record to support their arguments. In this case, we have only the arguments. The record is nearly nonexistent. Petitioner argues that he was a general partner with Willkie, Farr & Gallagher during 1986, and that this New York-based partnership's tax year ended in December. However, petitioner has offered no evidence in the record to establish either point. Petitioner argues that he filed his 1986 resident and nonresident personal income tax returns in full compliance with former Division regulation § 148.6, but, again, there is no evidence to support that fact either, because no returns were placed in evidence. Without the returns, we cannot determine how petitioner computed his tax. Accordingly, petitioner has failed to satisfy his burden of proof (Tax Law § 689[e]); 20 NYCRR 3000.15[d][5]). Without supporting evidence, petitioner's arguments are made in a vacuum, and must be rejected.

In any event, contrary to petitioner's arguments below, we held in ***Matter of Wertheimer*** (Tax Appeals Tribunal, January 12, 1995) that "the holding of ***McNulty*** is that where a partner's distributive share of income is reported without regard to actual receipt, the only possible method of allocation under section 654 is on a proportionate basis throughout the year."

Petitioner argues that the ***McNulty*** opinion permitted, but did not mandate, the proration of partnership income and losses. According to petitioner, the ***McNulty*** opinion created a rule of narrow application intended to redress inequitable results stemming from the application of regulation 148.6. Petitioner asserts that since he reported substantial income on his 1986 resident return, he suffered no loss of the benefit of exemptions and deductions as was the case in ***McNulty***. Based on this purported difference in the facts of the two cases, petitioner claims that application of regulation 148.6 does not lead to an inequitable result and must be permitted. This argument was raised and rejected by the Tribunal in our decisions in ***Matters of Wertheimer*** (Tax Appeals Tribunal, January 12, 1995 and March 14, 1996).

We note that the taxpayers in ***Wertheimer*** claimed that retroactively applying the ***McNulty*** decision to them would be unfair and inequitable. This petitioner argues that applying the holdings in ***McNulty*** and ***Wertheimer*** to him would be unfair or inequitable. Even if there was a factual basis for petitioner's argument, which there is not, we would disagree for the reasons stated in our two ***Wertheimer*** decisions. The determination of the Administrative Law Judge is affirmed for the reasons stated herein.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Bruce M. and Claire M. Montgomerie is denied;

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

3. The petition of Bruce M. and Claire M. Montgomerie is denied; and

4. The Notice of Disallowance dated December 30,1991 denying the claim for refund of taxes paid for 1986, is sustained.

DATED: Troy, New York

August 24, 2000

/s/Donald C. DeWitt
Donald C. DeWitt
President

/s/Carroll R. Jenkins
Carroll R. Jenkins
Commissioner

/s/Joseph W. Pinto, Jr.
Joseph W. Pinto, Jr.
Commissioner