STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
LOUIS E. AND FLORENCE R. FRIEDMAN	:	DECISION DTA NO. 816142
for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Years 1992 and 1993.	:	

Petitioners Louis E. and Florence R. Friedman, 7136 NW 103rd Avenue, Tamarac, Florida 33321-2274, filed an exception to the determination of the Administrative Law Judge issued on February 18, 1999. Petitioners appeared by Lloyd W. Winfield, CPA. The Division of Taxation appeared by Terrence M. Boyle, Esq. (Paul A. Lefebvre, Esq., of counsel).

Petitioners did not file a brief in support of their exception. The Division of Taxation filed a brief in opposition. Petitioners filed a reply brief. Oral argument, at petitioners' request, was heard on October 12, 1999 in New York, New York.

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

ISSUES

I. Whether wage income received by petitioner Florence R. Friedman, a nonresident, from Lo-Man Outdoor Store, Ltd. was for services performed entirely outside the State of New York and, thus, was not properly subject to New York State personal income tax.

II. Whether penalties imposed against petitioners pursuant to Tax Law § 685(b) and (p) should be sustained.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Petitioners, Louis E. Friedman and Florence R. Friedman, filed a New York State Nonresident and Part-Year Resident Income Tax Return (Form IT-203) for each of the years 1992 and 1993, indicating their filing status on each such return as "Married filing joint return." On their 1992 return, petitioners reported Federal line "1" income ("Wages, salaries, tips, etc.") of $100,700.00, and reported the New York amount of such income as $49,934.00. On their 1993 return, petitioners reported Federal line "1" income of $104,000.00, and reported the New York amount of such income as $51,352.00. Petitioners listed their address on each of these returns as 7136 Northwest 103rd Ave., Tamarac, Florida 33321 and indicated, by checking the "no" box at item "G" on the face of each return, that they did not maintain living quarters in New York State.

Forms W-2 ("Wage and Tax Statement") for each petitioner, as attached to their returns, indicate that petitioners' employer was Lo-Man Outdoor Store, Ltd. ("Lo-Man"), located in Babylon, New York, and that Mr. and Mrs. Friedman received wage income of $48,700.00 and $52,000.00, respectively, for 1992 (totaling $100,700.00 as reported), and $52,000.00 each for 1993 (totaling $104,000.00 as reported). These statements also indicate that Federal and New York State personal income tax, Social Security tax and Medicare tax was withheld from petitioners' wages for each year.

Each of petitioners' returns included an attached "Supplement to IT-203--Allocation of Wages and Salary Income to New York State," which presented a schedule by which each petitioner allocated to New York State a portion of his or her reported wage income from Lo-Man, as follows:

	1992	1993
Total days in year	366	365
Nonworking days[1]	(124)	(124)
Days worked	242	241
Days worked outside of New York State	(122)	(122)
Days worked in New York State	120	119

Petitioners used the ratio of days worked in New York State to total days worked in each year, as determined by the foregoing schedule, as the basis for allocating a portion of their reported wage income to New York, as follows:

Petitioner	Year	Wage Amount	Allocation Ratio	Wages Allocated to New York State
Louis R. Friedman	1992	$ 48,700.00	120/242	$24,149.00
Florence E. Friedman	1992	52,000.00	120/242	25,785.00
		$100,700.00		$ 49,934.00
Louis R. Friedman	1993	$52,000.00	119/241	$ 25,676.00
Florence E. Friedman	1993	52,000.00	119/241	25,676.00
		$104,000.00		$ 51,352.00

[1]For each year, nonworking days consisted of 104 Saturdays and Sundays, 10 holidays and 10 vacation days.

The Division of Taxation ("Division") conducted an audit of petitioners' returns for the years 1992 and 1993. This audit initially focused on whether petitioners were properly taxable as nonresidents of New York. Petitioners spent time in New York each year and, contrary to the information on the face of their returns, maintained a home in Bay Shore, New York. After examination, the auditor nonetheless concluded that petitioners, who had moved to Florida in or about 1981, were Florida domiciliaries and spent fewer than 183 days per year in New York State. Accordingly, petitioners were found to be properly taxable as nonresidents of New York. However, the auditor noted that petitioners continued to own Lo-Man, received wage income from such business, and reported a portion of such wage income as allocable to and taxable by New York State on the basis of the number of days worked in New York State over the total number of days worked in each year. Based on this manner of reporting, and because there was no evidence that petitioners performed services outside of New York State of necessity in the service of their employer, Lo-Man, rather than for their own convenience, the auditor concluded that all of petitioners' wage income was properly subject to tax by New York State.

Based on the foregoing audit results, the Division issued to petitioners a Statement of Personal Income Tax Audit Changes dated November 1, 1995. As is specifically relevant to the issue in this proceeding, the Division included the entire amount of petitioners' reported wage income for each of the years in question as properly subject to tax by New York State. Thus, the Statement reflects an "additional wage allocation" to New York in the amount of $50,766.00 for 1992 ($100,700.00 [total wages] less $49, 934.00 [reported allocated wages] equals $50,766.00), and in the amount of $52,648.00 for 1993 ($104,000.00 [total wages] less $51,352.00 [reported

allocated wages] equals $52,648.00).[2] The statement goes on to show the computation of additional tax due in the amounts of $4,012.58 for 1992 and $3,996.69 for 1993, and to include the assertion of a penalty for a deficiency due to negligence (Tax Law § 685[b]) and a penalty for substantial understatement of liability (Tax Law § 685[p]). The statement provides, with regard to the penalties, that "[a]s you maintained your NY home . . . but on your NYS return marked 'no' box sec. 685B and P penalties assessed."

The Division issued to petitioners a Notice of Deficiency, dated March 25, 1996, asserting additional personal income tax due for the years 1992 and 1993 in the aggregate amount of $8,009.27, plus penalties and interest. This notice parallels the Statement of Personal Income Tax Audit Changes and asserts the tax, penalties and interest determined to be due as the result of the above-described audit. Petitioners challenged the notice by requesting a conciliation conference with the Division's Bureau of Conciliation and Mediation Services ("BCMS"). In turn, the statutory notice was sustained by a Conciliation Order (CMS No. 155859) dated July 11, 1997, and petitioners continued their challenge by petitioning for a hearing before the Division of Tax Appeals.

On or about July 5, 1996 (i.e., after the issuance of the Notice of Deficiency), petitioners filed an amended Nonresident and Part-Year Resident Income Tax Return for each of the years in issue. These returns specify that the only amendments are to Item G, where petitioners have checked the "yes" box indicating that they did maintain living quarters in New York State during the years in question, and to their wage allocation. With regard to the latter item, petitioners

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[2]The Division's Statement also reflects IRA distributions ($9,559.00 for 1992 and $3,000.00 for 1993) and pension/annuity income ($2,000.00 for each year) as subject to tax by New York State. The propriety of these two audit adjustments has not been challenged by petitioners and is not in dispute.

have changed their reported wage allocation such that all of petitioner Louis E. Friedman's reported wage income is allocated to New York, and none of petitioner Florence R. Friedman's reported wage income is allocated to New York.[3]

Petitioners have owned Lo-Man for many years and are its sole shareholders, with each owning 50 percent of its stock. Lo-Man operates a retail establishment, selling various items including clothing and uniforms. Petitioners retired in or about 1981, and moved from New York to Florida. However, they continued to own Lo-Man, and it appears that petitioner Louis E. Friedman has remained actively involved in overseeing the operation of Lo-Man's business from the time of petitioners' move to Florida through and beyond the years in issue.

Lo-Man filed a U.S. Corporation Income Tax Return (Form 1120) for each of the years in issue. Schedule "E" ("Compensation of Officers") attached to each such return, lists each of the petitioners as owning 50 percent of the corporation's stock, as devoting 100 percent of their time to the business, and as receiving annual compensation of $52,000.00 each from the corporation. Consistently, line "12" of Lo-Man's Form 1120 lists a $104,000.00 deduction for compensation of officers for each of the years in issue.[4]

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[3]For 1992, the changed allocation schedule attached to petitioners' amended return shows the allocation of Mr. Friedman's entire $48,700.00 reported wage income to New York. This amount is, however, less than the $49,934.00 amount of wage income allocated by petitioners as reported on their returns as originally filed. Moreover, the latter $49,934.00 amount appears on the face of petitioners' amended return. For 1993, the changed allocation schedule reflects Mr. Friedman's entire $52,00.00 reported wage income as allocable to New York. This amount is greater than the $51,352.00 amount of wage income allocated by petitioners as reported on their returns as originally filed. Again, the originally allocated amount, rather than the amended allocated amount, appears on the face of petitioners' amended return. It would appear that these anomalies are the result of oversight or inadvertence accompanying the filing of the amended returns.

[4]As above, it is noted that the $104,000.00 total amount listed on Form 1120 for the year 1992 as compensation of officers is higher than the $100,700.00 amount of wage income reported for such year on petitioners' Form IT-203. Specifically, the $3,300.00 difference may be found from the fact that the Form W-2 issued to Mr. Friedman lists his wage income as $48,700.00, versus the $52,000.00 amount listed on Schedule "E"

(continued...)

Petitioners did not appear to give testimony at hearing. Instead, testimony was provided by petitioners' representative, and by Lo-Man's general manager and its office manager. According to the testimony of these individuals, and to an audit questionnaire completed and sworn to by petitioners, Lo-Man's day-to-day operations are handled by its general manager and its office manager, who are employed on-site at Lo-Man's store location in Babylon, New York.

Petitioners spend approximately nine months of each year in Florida (from mid-September to mid-June) and approximately three months of each year in New York (from mid-June to mid-September). Mr. Friedman remains involved throughout the year in overseeing Lo-Man's operations through telephone contact with Lo-Man's managers on a three-to-four call per week basis. During these calls, general business matters of any nature are discussed with Lo-Man's general manager and financial matters are discussed with Lo-Man's office manager. While Lo-Man's managers take care of all "hands-on" aspects of the business, they would specifically keep Mr. Friedman apprised of any unusual occurrence or problems.

The Friedmans' summer months were generally described as vacation time, during which they were based in New York and took trips including visits to their daughter in New England. During this time period, Mr. Friedman went to Lo-Man's retail location and worked in an office at that location. On the basis of this involvement and performance of services for Lo-Man at its New York location, and consistent with their amended returns, petitioners concede that all of Mr. Friedman's reported wage income from Lo-Man is properly allocable to and taxable by New York State. In this connection, petitioners admit that Mr. Friedman's work for Lo-Man while in

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[4](...continued)
of the Lo-Man corporate income tax return for 1992. As above, this discrepancy is not addressed or explained in the record.

Florida, which was performed at petitioners' home in Florida, was not performed there of necessity in the service of Lo-Man but rather was performed there as Mr. Friedman's choice and for his convenience. While petitioners' representative alluded to the existence of a separate office in petitioners' home in Florida, the record provides no description or other specifics concerning such an office. Any expenses incurred, such as telephone, travel, postage, stationery, and the like are included as expenses on Lo-Man's corporation income tax returns. In this regard, petitioners' representative explained that there is no separate segregation or statement on such returns for an office in Florida, noting that the dollar amounts of the expenses are not, comparatively, significant.

Petitioners' position with respect to Florence R. Friedman is that she performs no services for Lo-Man during the period of time when petitioners are in New York State, and instead receives compensation for her duties only when she is in Florida. In this regard, petitioners' witnesses testified that Mrs. Friedman does not telephone them at the Lo-Man store premises, and performs no work at the store. Petitioners' witnesses also stated that the wage income paid to Mrs. Friedman was not based on any specific hours worked or duties performed by her on a regular basis, but instead that the wage amounts paid to both Mr. and Mrs. Friedman were simply determined to be "appropriate" salary amounts based on the profitability of the business. In fact, petitioners' witnesses could not describe or specify any particular services performed by Mrs. Friedman for Lo-Man, or any instances where they consulted Mrs. Friedman concerning any aspect of Lo-Man's business, either when she was in Florida or in New York State. Petitioners' representative alleged that Mrs. Friedman was compensated by Lo-Man for holding corporate office and for being available to be consulted when corporate decisions had to be made, noting

that as an owner and officer of the corporation she has the right to be consulted in such instances. Petitioners' representative admitted that any such consultations were infrequent, occurring "possibly" two or three times per year. No particular instances of consultation or involvement were described, except for one reference to a meeting several years prior to the years in issue concerning the implementation of a profit sharing plan by Lo-Man. Lo-Man's Federal income tax returns list Mrs. Friedman as an officer, on Schedule "E" titled "Compensation of Officers," and petitioners' representative claimed that Mrs. Friedman was an officer of the corporation. However, the record does not further disclose the particular corporate officer title held by Mrs. Friedman.

At hearing, petitioners admitted that they were audited on this same issue of their manner of allocation of reported wage income for certain years prior to those at issue herein, and that a Notice of Deficiency was issued based on the Division's reallocation of all wage income received by petitioners as subject to New York State personal income tax. These prior year audit results were conceded, and the resulting asserted tax deficiencies were paid by petitioners, allegedly because the dollar amounts were less significant than those at issue herein.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge reviewed applicable provisions of the Tax Law and Commissioner's regulations concerning the definition of New York source income of a nonresident and the method of allocating income and deductions from sources within and without New York State. The Administrative Law Judge accepted petitioners' concession that the wage income paid by Lo-Man to petitioner Louis E. Friedman was fully allocable to and taxable by New York State because he performed services for Lo-Man both in New York State

and at his home in Florida, and that the services he performed for Lo-Man at his home in Florida were performed there as a matter of choice or convenience to petitioner Louis E. Friedman rather than out of necessity for Lo-Man.

The Administrative Law Judge rejected, however, petitioners argument that none of the wage income paid to petitioner Florence R. Friedman by Lo-Man was allocable to or taxable by New York State because she performed no services for Lo-Man in New York State and was only compensated for services performed for Lo-Man while she was in Florida. The Administrative Law Judge found that Mrs. Friedman performed no specific services for Lo-Man clearly identifiable to either Florida or New York State but received compensation for holding corporate office and for being available for consultation year round. The Administrative Law Judge did not accept petitioners' argument that Mrs. Friedman was consulted only in Florida, but was unavailable to do so or refused to do so for the three-month period of each year when she and Mr. Friedman were in New York State. As a result, the Administrative Law Judge concluded that at least a portion of her wage income must be considered to have been earned during the period when she was in New York State holding corporate office and remaining available for consultation. The Administrative Law Judge concluded that such income was properly treated as derived from or connected to New York sources and was properly allocable to and taxable by New York State.

The Administrative Law Judge observed that case law has established that services performed at an out-of-State home, which could have been performed at the employer's in-State office, are performed for the employee's convenience and not for the employer's necessity. In this case, Mrs. Friedman performed no discernable services other than holding corporate office

and being available for consultation year round, when and if needed, whether within or without New York State. The Administrative Law Judge concluded that the most appropriate method of allocating petitioner Florence R. Friedman's income would be on the basis of time spent in New York State versus time spent in Florida over the course of the entire year, rather than on the basis of the number of days "worked" within and without New York. However, in order to allow for any allocation of wage compensation, the Administrative Law Judge noted that it must first be shown that Mrs. Friedman performed services for her employer at her home in Florida of necessity rather than for her own convenience. The Administrative Law Judge found no basis in the record upon which to conclude that the services for which Mrs. Friedman was compensated were required to be performed at petitioners' home in Florida rather than in New York. Thus, the Administrative Law Judge concluded that petitioner Florence R. Friedman could not apportion and allocate any of her compensation from Lo-Man to Florida. Rather, her compensation was fully allocable to and taxable by New York State.

The Administrative Law Judge found that petitioners advanced no grounds warranting the abatement of penalties imposed in this case. The allocation of their income was the subject of a prior audit. Further, petitioners agreed in the present case that they did not properly allocate Mr. Friedman's wage income for the years in question, conceding that he, in fact, performed services for Lo-Man in New York State and that none of the services he performed for Lo-Man in Florida were performed there of necessity for his employer rather than for his own convenience or as a matter of personal choice.

ARGUMENTS ON EXCEPTION

On exception, petitioners argue that unless a nonresident employee actually performs services for the employer within New York State, none of that employee's compensation should be taxed by New York State. Petitioners assert that the Administrative Law Judge erroneously failed to accept the testimony of petitioners' witnesses that Mrs. Friedman performed no employee functions within New York State during her visit here for three months of the year. Petitioners state that there was no testimony introduced by the Division to controvert petitioners' evidence. Finally, petitioners argue that their consent to the findings of a prior audit should not be the basis for assertion of penalty in the present case.

The Division argues that the Administrative Law Judge's determination was correct. While petitioners' witnesses testified that Mrs. Friedman performed no services at the employer's location in New York State, the Division asserts that no explanation was provided as to the nature of services Mrs. Friedman did perform that justified her annual salary. The Division agrees with the Administrative Law Judge that there was no evidence to support a conclusion that the services rendered by Mrs. Friedman were only performed outside of New York or that such services were performed outside of New York State as a matter of corporate necessity rather than for the convenience of the employee. Finally, the Division argues that penalty was properly imposed on petitioners because the issue of allocation of petitioners' income had been resolved against petitioners in a previous audit. Petitioners presented no evidence that Mrs. Friedman's failure to properly allocate the income at issue to New York State was reasonable.

OPINION

We affirm the determination of the Administrative Law Judge. Petitioners have raised the same issues and presented the same arguments herein as were considered by the Administrative Law Judge. We find that the Administrative Law Judge completely and adequately addressed the issues presented to him and correctly applied the Tax Law and relevant case law to the facts of this case. We see no reason to modify his determination in any respect.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Louis E. and Florence R. Friedman is denied;

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

3. The petition of Louis E. and Florence R. Friedman is denied; and

4. The Notice of Deficiency, dated March 25, 1996, is sustained.

DATED: Troy, New York
March 2, 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