

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
ROBERT G. BAUER AND JOAN C. BAUER	:	DETERMINATION
for Redetermination of a Deficiency or for	:	DTA NO. 811537
Refund of Personal Income Tax under Article 22	:	
of the Tax Law for the Year 1985.	:	

Petitioners, Robert G. Bauer and Joan C. Bauer, 132 Marvin Street, Patchogue, New York 11772, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the year 1985.

A hearing was held before Timothy J. Alston, Administrative Law Judge, at the offices of the Division of Tax Appeals, Riverfront Professional Tower, 500 Federal Street, Troy, New York, on June 7, 1994 at 1:15 P.M. The Division of Taxation submitted additional evidence on June 21, 1994. Petitioners submitted additional evidence and a brief on July 25, 1994. The Division of Taxation submitted a letter brief on September 9, 1994. Petitioners submitted a reply brief on October 10, 1994. Petitioner Robert G. Bauer appeared pro se and on behalf of his wife, Joan C. Bauer. The Division of Taxation appeared by William F. Collins, Esq. (Michael J. Glannon, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly determined that petitioners received, in 1985, shares in a cooperative housing corporation and an ownership interest in a co-op apartment as compensation for legal services rendered by petitioner Robert Bauer.

FINDINGS OF FACT

On January 22, 1991, the Division of Taxation ("Division") issued to petitioners, Robert G. Bauer and Joan C. Bauer, a Notice of Deficiency which asserted \$13,797.28 in additional personal income tax due, plus penalties and interest, for the year 1985.

A Statement of Personal Income Tax Audit Changes dated October 16, 1990 indicated that the tax liability asserted against petitioners was "based on value of co-op apartment as undeclared income." The statement listed additional income of \$106,800.00 to petitioners as the value of such co-op apartment.

The Statement of Audit Changes also indicated that penalties were being asserted against petitioners for failure to timely file a return (Tax Law § 685[a][1][A]); failure to pay tax shown on return (Tax Law § 685[a][2]); deficiency due to negligence (Tax Law § 685[b]); failure to pay estimated tax (Tax Law § 685[c]); and substantial understatement of liability (Tax Law § 685[p]).

Petitioners late filed their joint 1985 New York State personal income tax return (Form IT-201) on September 17, 1990. With their return petitioners remitted a payment of \$3,830.05.

Attached to petitioners' 1985 New York return was a depreciation schedule listing property depreciated on petitioners' 1985 Federal Schedule E ("Supplemental Income Schedule"). Among the property listed on the depreciation schedule was "Condo-Hermitage" with an acquisition date listed of "1/85" at a cost of \$20,000.00.¹ Also attached to petitioners' 1985 return was a copy of Mr. Bauer's Schedule C for his law practice, which indicated that Mr. Bauer used a cash accounting method.

A copy of a portion of petitioners' 1986 Federal income tax return was also entered into evidence herein. Schedule D of said return ("Capital Gains and Losses") listed a \$6,000.00 long-term capital loss resulting from the sale of a "condo" acquired "1/85" at a cost of \$106,000.00 and sold "12/86" at a price of \$100,000.00.

On audit, the Division determined that, in lieu of legal fees, petitioner Robert Bauer had received a cooperative apartment unit located at "The Hermitage at Napeague", Amagansett, New York and that the fair market value of this unit was properly reportable as ordinary income. Upon review of petitioners' 1985 New York return and 1986 Federal return, the

¹The record contains no explanation for this \$20,000.00 cost figure.

Division determined that petitioners had acquired the cooperative unit in January 1985 and that the unit's fair market value at that time was \$106,800.00. The Division also observed that petitioners had not reported this \$106,800.00 on their 1985 New York return. The Division concluded, therefore, that petitioners had improperly failed to report the value of the cooperative unit on their 1985 return and issued the aforementioned Statement of Personal Income Tax Audit Changes and Notice of Deficiency accordingly.²

At all times relevant herein, petitioner Robert G. Bauer was engaged in the practice of law as a sole practitioner. Commencing in or about 1968, petitioner began representing a Mr. Kenneth J. Tedaldi in connection with numerous real estate acquisition and development activities undertaken by Mr. Tedaldi. In September 1981, Mr. Tedaldi, acting through a corporate entity called Kenneth J. Tedaldi, Inc., acquired a parcel of real property in Amagansett, New York ("the Amagansett property"). Mr. Tedaldi intended to develop the Amagansett property by constructing condominium-type units.

Throughout 1982, architectural plans for the development of the Amagansett property were drawn and efforts were made to secure the requisite governmental approvals. On November 3, 1982, a building permit was granted to Mr. Tedaldi for the construction of 56 "motel units" on the Amagansett property.

In September 1982, Napeague Dunes Development Corporation ("Napeague Dunes") was incorporated. Mr. Tedaldi was president and petitioner Robert Bauer was secretary of this corporation. Pursuant to a contract of sale dated December 15, 1982 and a deed dated March 30, 1983, title to the Amagansett property was transferred from Kenneth J. Tedaldi, Inc. to Napeague Dunes Development Corporation. Mr. Bauer signed the December 15, 1982 contract on behalf of Napeague Dunes Development Corporation.

²It appears that the Division erred in its determination that the value of the coop was \$106,800.00 (see, Finding of Fact "2"), since the 1986 Federal return, upon which the Division's determination was based, lists a cost for the unit of \$106,000.00.

In March 1983, The Hermitage at Napeague, Ltd. ("The Hermitage") was incorporated. Mr. Tedaldi was president of this corporation and petitioner Robert Bauer was secretary.

By deed dated February 2, 1984, title to the Amagansett property was transferred from Napeague Dunes Development Corporation to The Hermitage.

Napeague Dunes Development Corporation was the sponsor of a conversion of the Amagansett property, as developed, to cooperative ownership and The Hermitage was the cooperative housing corporation.

Petitioner Robert Bauer provided legal services to Napeague Dunes Development Corporation and The Hermitage in connection with their incorporation and in connection with the real property transfers referred to in Findings of Fact "8", "10", and "12". Petitioner also provided legal services in connection with the application for a building permit and also in connection with The Hermitage's filing of an offering plan to convert the Amagansett property to cooperative ownership with the New York State Attorney General's office.

Petitioners made use of one of the cooperative units, Unit D-12, at The Hermitage during 1984. Such use included furnishing the unit, rental of the unit during the summer months, and personal use. In connection with the rental of Unit D-12, petitioners took out an advertisement in the New York Times offering the unit for summer rental.

During 1984, petitioners received statements from the management of The Hermitage with respect to their rental of Unit D-12. Such statements listed receipts paid to the managing agency for the rental of the unit, less taxes, expenses and a management fee, and listed a payment amount due petitioners. Petitioners also received general correspondence from the management of The Hermitage addressed "Dear Shareholder".

Petitioners purchased a "condominium" insurance policy for Unit D-12 which covered the period May 30, 1984 through May 30, 1985. Said policy insured petitioners' personal property for \$10,000.00.

Pursuant to a stock certificate dated January 10, 1985, petitioners received 160 shares of The Hermitage.

Petitioners submitted into the record a letter dated June 10, 1983 written by Mr. Bauer and addressed to Mr. Tedaldi which stated:

"I wanted to outline our understanding regarding the arrangements for my final fee in connection with the above.

"As of now, I have one share of stock of Napeague Dunes Development Corp. and you have 50 shares. This was given to me in November, 1982 as my fee. The understanding is that in November 1983, after one year, you will be obligated to allow me to transfer that share of stock to you in return for ownership of one unit, of your choosing, in the Hermitage. Thereafter you will agree to carry the full maintenance on the unit for one year. At that point, November of 1984, you will owe me an additional \$40,000. If I keep the unit, you will have the option of either paying me the \$40,000. or pay the monthly maintenance charges for me until you have paid the \$40,000. on my behalf to the Hermitage Co-op.

"If I sell the unit at any time prior to your paying me the full \$40,000., you will be obligated to pay me the balance due on the \$40,000. on terms to be agreed upon.

"All of this is on the understanding that the stock transfer is in consideration of \$150,000. as of November 1983. So that I am getting with a \$160,000. unit, \$110,000. free and clear with the underlying co-op mortgage of \$50,000. of which you owe me \$40,000.

"If this is agreeable, please counter-sign the enclosed copy and return it to me."

Mr. Tedaldi's signature was not contained on the copy of the letter submitted in evidence herein.

SUMMARY OF THE PARTIES' POSITIONS

The Division asserted that petitioners received 160 shares in The Hermitage in January 1985 and that, upon receipt of such shares, acquired an ownership interest in Unit D-12. The Division asserted that the value of such shares was \$106,000.00 based upon information contained on petitioners' 1986 Federal income tax return.

Petitioners contended that Mr. Bauer and Mr. Tedaldi entered into an oral "co-venture" agreement in 1981 to develop the Amagansett property into cooperative apartments. Petitioners further contended that, pursuant to this "co-venture" agreement, corporate stock was issued to petitioners in 1983 by Napeague Dunes Development Corporation and that that stock was converted into ownership of cooperative Unit D-12 in 1984. Petitioners asserted that the Napeague Dunes stock issued to them in 1983 had value and therefore constituted taxable income in 1983. At the least, petitioners asserted, the taxable event occurred in 1984 when they

took possession of Unit D-12. Petitioners further asserted that the delivery of the shares of The Hermitage in 1985 was merely a ministerial act, with all the essential terms of the co-venture agreement having been fulfilled prior to 1985. Petitioners reasoned that since any income to petitioners was realized prior to 1985, the Division's assessment of tax due for 1985 was improper. Moreover, petitioners argued, the years in which the income was realized and therefore reportable, i.e., 1983 or 1984, are beyond the three-year period of limitations for assessment.

CONCLUSIONS OF LAW

A. For cash basis taxpayers, items of income are generally reportable and taxable in the year in which they are actually or constructively received (see, IRC § 451[a]; Treas Reg § 1-451-1[a]). Tax Law § 683(a) generally imposes a three-year period of limitations on assessment. Petitioners' 1985 New York State personal income tax return was filed on September 17, 1990. The Notice of Deficiency herein is dated January 22, 1991. Said notice is therefore timely if it is determined that petitioners received their ownership interest in The Hermitage in 1985. The Notice of Deficiency would be untimely if petitioners received their ownership interest prior to 1985.

B. Petitioners' claim that Mr. Bauer and Mr. Tedaldi were involved in a "co-venture"³ is rejected. With respect to this claim, it is noted that the June 10, 1983 letter refers to "the arrangements for [Mr. Bauer's] final fee." There is no reference in the letter to any "co-venture"; nor does the record contain any evidence that Mr. Tedaldi considered their arrangement to be a "co-venture". Furthermore, although Mr. Bauer was an officer of Napeague Dunes and The Hermitage, other than his signature on one contract (see Finding of Fact "10"), there is no evidence that Mr. Bauer had any responsibilities as such an officer. Accordingly, it is concluded that Mr. Bauer and Mr. Tedaldi did not enter into a "co-venture" arrangement with

³It is presumed that by the term "co-venture" petitioners refer to a business arrangement commonly known as a joint venture. Petitioners have provided no further explanation of this term.

respect to the development of the Napeague Dunes property. Rather, the record herein establishes that Mr. Bauer was to receive shares in the cooperative and an interest in an apartment unit as his fee for legal services rendered.

C. Petitioners have failed to prove that income earned by Mr. Bauer in connection with legal services provided in relation to The Hermitage cooperative conversion was received in 1983 or 1984.

With respect to petitioners' contention, supported primarily by Mr. Bauer's testimony, that such income was received in 1983 upon the asserted transfer of one share of Napeague Dunes stock to Mr. Bauer, upon review of the record herein, it is concluded that petitioners have not shown that such a transfer, in fact, occurred. Weighing strongly against petitioners on this point is their failure to produce a copy of the share

certificate or any other Napeague Dunes records indicating the issuance of a share of stock to Mr. Bauer. Nor did petitioners produce Mr. Tedaldi, the individual in control of Napeague Dunes, to testify with respect to such a stock transfer. Moreover, the weight to be accorded the June 10, 1983 letter in which Mr. Bauer asserts ownership of the share is diminished by the lack of any evidence in the record indicating that Mr. Tedaldi consented to the terms for Mr. Bauer's final fee as outlined in the letter. Additionally, and contrary to petitioners' general and conclusory testimony, it is not at all clear that Mr. Tedaldi complied with the terms of the June 10, 1983 letter. Specifically, contrary to the letter The Hermitage shares were not transferred until 1985; the coop unit was apparently worth \$106,000.00 and not \$160,000.00 as indicated by the letter; and there is no evidence in the record that specifically indicates Mr. Tedaldi paid petitioners \$40,000.00 as provided in the letter.

With respect to petitioners' contention that, at the latest, the income in question was realized in 1984, it is noted that the record herein does establish petitioners' use of and rental of the condominium unit during that year. The record does not establish, however, that petitioners were shareholders of The Hermitage during 1984.

Petitioners assert that the only logical explanation for their use and rental of the condominium and receipt of correspondence from the condominium's management in 1984 is that petitioners were, in fact, shareholders of The Hermitage during 1984. This contention is rejected. While petitioners' explanation is one logical inference one could draw from the instant circumstances, the evidentiary inconsistencies and gaps in the record necessarily prevent petitioners from establishing, pursuant to their burden of proof (Tax Law § 689[e]), that they were shareholders of The Hermitage in 1984. Specifically, the share certificate dated January 10, 1985 and the 1985 and 1986 tax returns in evidence explicitly and directly indicate that petitioners became shareholders in 1985. In contrast, the documentation submitted by petitioners does not directly establish ownership of shares in The Hermitage prior to 1985. Clearly, therefore, petitioners' evidence is outweighed by the documentation supportive of the Division's position.

Also significant is the absence from the record of a proprietary lease which might have given some indication of when petitioners became shareholders. Additionally, corporate records of The Hermitage would likely indicate when petitioners became shareholders, but no such records were introduced. Finally, the June 10, 1983 letter refers to a "coop mortgage of \$50,000." This document, if it exists, might also have proven useful in establishing when petitioners became shareholders.

Mr. Bauer's testimony in support of petitioners' position amounts to a contention that petitioners owned shares of The Hermitage worth \$106,000.00 prior to 1985, but lacked any documentation to prove such ownership. Even allowing for Mr. Bauer's long professional relationship with Mr. Tedaldi, such a set of circumstances would be difficult to accept absent a compelling explanation and no such explanation has been offered herein. Given the stock certificate dated January 10, 1985 and the tax returns in evidence, it is concluded that the testimony is insufficient to establish petitioners' contention.

D. The Division is directed to adjust the subject Notice of Deficiency in accordance with footnote "2" herein. That is, to reflect a value of \$106,000.00 for the coop shares as reported on

petitioners tax returns and not \$106,800.00 as asserted by the Division.

E. Except as noted in Conclusion of Law "D", the petition of Robert G. Bauer and Joan C. Bauer is denied and the Notice of Deficiency, dated January 22, 1991, is sustained.

DATED: Troy, New York
March 16, 1995

/s/ Timothy J. Alston
ADMINISTRATIVE LAW JUDGE