STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
BRUCE AND MARNI GUTKIN	:	ORDER DTA NOS.
for Redetermination of Deficiencies or for Refund of New York State and New York City Personal Income Taxes under Article 22 of the Tax Law and the New York City Administrative Code for the Years 2005 and 2006.	:	822657 AND 822658

Petitioners, Bruce and Marni Gutkin, filed petitions for redetermination of deficiencies or for refund of New York State and New York City personal income taxes under Article 22 of the Tax Law and the New York City Administrative Code for the years 2005 and 2006.

Petitioners, appearing by Schoeman, Updike & Kaufman, LLP (David B. Gordon, Esq., of counsel), brought a motion dated January 12, 2009, including therewith affidavits made by counsel and by petitioner Bruce Gutkin, supporting documents, and a memorandum of law, seeking an order granting summary determination in petitioners' favor pursuant to Tax Law § 2006(6) and 20 NYCRR 3000.9(b). On March 26, 2009, the Division of Taxation by its representative Daniel Smirlock, Esq. (Kevin R. Law, Esq., of counsel), submitted a responding affirmation by counsel and an affidavit made by Cheryl Catman, including supporting documents, and a memorandum of law, in opposition to the motion for summary determination. Petitioners, pursuant to permission granted, submitted a reply affidavit made by petitioner Bruce Gutkin and a reply memorandum of law in support of the motion on April 30, 2009, which date commenced the 90-day period for issuance of this order.

After due consideration of the motion and supporting papers, the papers filed in opposition thereto, the reply papers, and all pleadings and proceedings had herein, Dennis M. Galliher, Administrative Law Judge, renders the following order.

ISSUE

Whether the Division of Taxation improperly issued notices of deficiency disallowing certain losses claimed on Schedule E to petitioners' personal income tax returns for the years 2005 and 2006 upon the premise that the claimed losses arose as the result of improper tax avoidance transactions (oil and gas drilling expenses of certain partnerships) thereby warranting dismissal of such notices of deficiency.

FINDINGS OF FACT

1. In 2001, petitioner Bruce Gutkin acquired interests in certain partnerships known as Gulf Coast Drilling Company II (GCDC II) and Gulf Coast Drilling Company III (GCDC III), paying in the aggregate $1.4 million in cash and $2.52 million in promissory notes. In 2002, petitioner Bruce Gutkin acquired an interest in a partnership known as Gulf Coast Drilling Company IV (GCDC IV), paying $1.2 million in cash and $2.16 million via a promissory note.

2. Petitioners, Bruce and Marni Gutkin, filed Form IT-201, New York State and City of New York resident income tax returns, for each of the years 2001 through 2006, including an amended return (Form IT-201-X) for the year 2001. On these returns, petitioners claimed losses as set forth on Schedule E (Supplemental Income and Loss [From rental real estate, royalties, partnerships, S corporations, estate, trusts, REMICs, etc.]). A portion of the total claimed losses were attributable to the partnerships noted above.

3. On September 5, 2008, the Division of Taxation (Division) issued to petitioners notices of deficiency for each of the years 2001 through 2006. Thereafter, petitioners timely filed

petitions challenging the notices of deficiency for each of the years 2001 through 2006, and the Division duly filed its answers thereto.

4. In turn, petitioners brought the subject motion for summary determination and dismissal of the notices of deficiency for all of the years 2001 through 2006. However, petitioners have withdrawn their petitions for the years 2001 through 2004, premised upon their election to participate in the Voluntary Compliance Initiative (L 2008, ch 57, Part CC-1) for such years, thus leaving only the years 2005 and 2006 remaining at issue herein.

5. The notices of deficiency for 2005 and 2006 each consist of four pages (front and back of two pages) and set forth identical information in the "Explanation and Instructions" and "Computation Section" portions thereof, save for different dollar amounts on each, since different years and thus different amounts of income, gain, loss and deduction are involved.

a) In relevant part, the Explanation and Instructions portion of each notice provides:

> Based on an audit, an additional amount is due for the Tax Type indicated above. Please refer to the COMPUTATION SECTION and/or COMPUTATION SUMMARY SECTION for the tax period(s) affected, the reason(s) for the additional amount due and a computation of the balance due.

b) In relevant part, the Computation Section portion of each notice provides:

> Your [tax year] New York State tax return was selected for *review*. The recomputation of your return has resulted in additional New York State and New York City and/or Yonkers tax due.
>
> The audit of your New York State returns covers more than one year. A separate bill will be issued for each individual tax year. You may not receive all of the bills on the same day.
>
> *You failed to provide the requested documentation regarding your basis in Gulf Coast Drilling Co. II . . . and Gulf Coast Drilling Co. IV . . . . Therefore, we are disallowing the loss you claimed on Federal Schedule E in the amount of* [$437,113 (for 2005) and $593,955 (for 2006)]. (Emphasis added.)

6. Each of the notices of deficiency goes on to set forth the allowance of itemized deductions and the resident credit, and to explain the statutory sections pursuant to which the imposition and calculation of various penalties and interest set forth on the notices were premised. Thereafter, the notices provide the telephone number and name of a person, Elvin Vicens, to contact with any questions. Finally, the notices each set forth numeric calculations by which the amounts of the asserted deficiencies were arrived at for each year, to wit, additional state and city tax in the aggregate amounts (excluding penalties and interest) of $53,343.56 for 2005 and $62,510.06 for 2006.

7. Review of petitioners' 2005 Form IT-201 reveals a reported Schedule E loss claimed in the amount of $424,787.00. Review of Schedule E for 2005 reveals this amount consisted of the net of petitioner Bruce Gutkin's aggregate reported passive loss amount ($4,810.00) plus aggregate nonpassive loss amount ($432,303.00), totaling $437,113.00, less his aggregate reported passive income amount of $12,326.00.[1] Review of Statement 5 to Schedule E of petitioners' return shows the same total amounts of income and loss, in the aggregate, for all of the entities listed thereon, and also shows that the three partnerships GCDC II, GCDC III and GCDC IV listed nonpassive losses in the respective amounts of $13,500.00, $35,126.00 and $122,279.00, with no passive losses, passive income or nonpassive income shown for any of such entities.

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[1] It is noted that the Division disallowed the "loss" reported on Schedule E in the amount of $437,113.00, which amount represents the *total* amount of loss (passive and nonpassive) reflected on Schedule E and shown by Statement 5 as reported for all of the entities listed on Statement 5. This amount differs from the *net* amount of loss reported on Schedule E and on Form IT-201 (i.e., $424,787.00 consisting of the net of the passive and nonpassive loss and passive and nonpassive income) reflected on Schedule E and shown by Statement 5 as reported for all of the entities listed on Statement 5.

8. Review of petitioners' 2006 Form IT-201 reveals a reported Schedule E loss claimed in the amount of $593,955.00. Review of Schedule E for 2006 reveals this amount consisted of the net of petitioner Bruce Gutkin's aggregate reported passive loss amount ($27,803.00) plus aggregate nonpassive loss amount ($813,189.00), totaling $840,992.00, less his aggregate reported passive income amount of $5,560.00, plus his aggregate nonpassive income amount of $241,474.00, totaling $247,034.00. Review of Statement 3 to Schedule E of petitioners' return shows the same total amounts of income and loss, in the aggregate, for all of the entities listed thereon, and also shows that the three partnerships GCDC II, GCDC III and GCDC IV listed nonpassive losses in the respective amounts of $132,615.00, $42,613.00 and $119,842.00, with no passive losses, passive income or nonpassive income shown for any of such entities.

9. Petitioners point out, in seeking summary determination, that the amounts of loss disallowed by the Division actually exceed the amounts of loss that petitioners claimed on Schedule E for GCDC II and GCDC IV for the years in issue, thus positing that the amounts of additional tax asserted as due are inaccurate and incorrect. Petitioners also claim that there was no audit of their returns conducted prior to issuance of the notices of deficiency, and dispute the Division's allegation that petitioners failed to provide the requested documentation regarding their basis in the entities. In this regard, petitioners' counsel claims, in his affidavit in support of the motion, that he contacted the Division's auditor, Elvin Vicens, by telephone on multiple occasions to discuss the requests for the production of documents, advising that petitioners were "attempting to gather the requested materials and intended to produce them to the extent that they possessed them." Petitioners' counsel also states that he discussed with Mr. Vicens the nature of the materials being forwarded, offered to "walk Mr. Vicens through them", and "told Mr. Vicens that he should call me if he wanted any additional documents." On a later telephone contact,

petitioners' counsel asked Mr. Vicens if he "needed anything else and/or wanted any help in interpreting the documents he received, and Mr. Vicens indicated that he would be in touch when or if he needed anything." There was apparently no additional contact between petitioners' counsel and Mr. Vicens prior to issuance of the notices of deficiency.

10. In her affidavit, Tax Technician Cheryl Catman states that the notices were issued disallowing Schedule E losses from GCDC II, GCDC III and GCDC IV as claimed on petitioners' tax returns for 2005 and 2006. Ms. Catman states that the disallowances were based on the Division's belief that the entities are tax shelters. She points, in this regard, to "Investment Proposals" promoting and describing the structure of each of the three entities, obtained directly from the entities' promoter, Brad Reiss. Ms. Catman also states that subsequent to the issuance of the notices of deficiency, the same were adjusted by reducing the amounts of loss originally disallowed by the amount of any interest income from each entity reported on petitioner Bruce Gutkin's forms K-1 over and above cash distributions to Mr. Gutkin from the entities. Ms. Catman thus states that the Division (pursuant to Internal Revenue Code [IRC] § 461) has only allowed losses from the entities to the extent of Mr. Gutkin's cash basis in such entities. Accompanying Ms. Catman's affidavit were the Investment Proposals and the noted calculation adjustments which reflect reductions in the amounts of tax asserted as due from $53,353.56 to $15,093.60 (for 2005) and from $62,510.06 to $21,359.86 (for 2006), exclusive of penalties and interest. Ms. Catman notes in her affidavit that petitioners have paid these revised amounts.

11. Prior to the filing of answers to the petitions at issue herein, the Division's counsel e-mailed revised calculations of the notices of deficiency, as prepared by Ms. Catman, to petitioners' counsel. The Division's answers to the petitions in these matters, dated February 11, 2009, further specify the basis for and calculation of the asserted deficiencies.

12. Petitioner Bruce Gutkin, in his reply affidavit, denies having seen or relied upon the investment proposals referenced by Ms. Catman as supporting the Division's belief that the GCDC entities were tax shelters, and claims that his investments in such entities were motivated solely by his desire to make money by investing in entities involved or engaged in the oil and gas industry.

CONCLUSIONS OF LAW

A. Any party appearing before the Division of Tax Appeals may bring a motion for summary determination as follows:

> Such motion shall be supported by an affidavit, by a copy of the pleadings and by other available proof. The affidavit, made by a person having knowledge of the facts, shall recite all material facts and show that there is no material issue of fact, and that the facts mandate a determination in the moving party's favor. (20 NYCRR 3000.9[b][1]; ***see also*** Tax Law § 2006[6].)

The standard in reviewing a motion for summary determination is well established and has been articulated many times. An administrative law judge is initially guided by the following regulation:

> The motion shall be granted if, upon all papers and proof submitted, the administrative law judge finds that it has been established sufficiently that no material and triable issue of fact is presented and that the administrative law judge can, therefore, as a matter of law, issue a determination in favor of any party. The motion shall be denied if any party shows facts sufficient to require a hearing of any material and triable issue of fact. (20 NYCRR 3000.9[b][1]; ***see also*** Tax Law § 2006[6].)

Furthermore, a motion for summary determination made before the Division of Tax Appeals is "subject to the same provisions as motions filed pursuant to section three thousand two hundred twelve of the CPLR." (20 NYCRR 3000.9[c]; ***see also Matter of Service Merchandise, Co.***, Tax Appeals Tribunal, January 14, 1999.) Summary determination is a "drastic remedy and should not be granted where there is any doubt as to the existence of a triable issue" (***Moskowitz v. Garlock***,

23 AD2d 943, 259 NYS2d 1003, 1004 [1965]; ***see Daliendo v. Johnson***, 147 AD2d 312, 543 NYS2d 987, 990 [1989]). Because it is the "procedural equivalent of a trial" (***Museums at Stony Brook v. Village of Patchogue Fire Dept.***, 146 AD2d 572, 536 NYS2d 177, 179 [1989]), undermining the notion of "a day in court," summary determination must be used sparingly ***(Wanger v. Zeh***, 45 Misc 2d 93, 256 NYS2d 227, 229, ***affd*** 26 AD2d 729 [1966]). It is not for the court "to resolve issues of fact or determine matters of credibility but merely to determine whether such issues exist" (***Daliendo v. Johnson***, 543 NYS2d at 990). If any material facts are in dispute, if the existence of a triable issue of fact is "arguable," or if contrary inferences may be reasonably drawn from undisputed facts, the motion must be denied (***Gerard v. Inglese***, 11 AD2d 381, 206 NYS2d 879, 881 [1960]).

B. Petitioners' maintain that their motion should be granted and the notices of deficiency canceled because, as issued, the notices assert amounts of loss claimed by petitioners with respect to the GCDC entities which exceed the amounts of loss actually claimed with respect to such entities, thereby rendering the dollar amounts of the deficiencies inaccurate, incorrect and, allegedly, invalid. Petitioners also maintain that the notices were issued without an audit of petitioners' returns, and thus lack a rational basis, and that such notices fail to provide petitioners with sufficient information to enable the preparation of a defense thereto. Petitioners further assert that to the extent the Division relied upon the Investment Proposals in concluding the GCDC entities were tax shelters, the same constitute hearsay, were not seen by petitioner Bruce Gutkin prior to investing, were thus not relied upon by him and did not constitute any part of his motivation in making his investment decision, and may not be relied upon by the Division.

C. From all the evidence submitted on this motion, there is no doubt that material and triable issues of fact exist. Accordingly, petitioners' motion for summary determination and

dismissal of the notices of deficiency must be denied. Petitioners' primary claim is that the Division did not conduct an audit of their returns, and thus the notices of deficiency are invalid as lacking a rational basis to support their issuance. Tax Law § 681(a) provides that "[i]f upon examination of a taxpayer's return under [Article 22] the tax commission determines that there is a deficiency of income tax, it may mail a notice of deficiency to the taxpayer." Petitioners' claim that no audit (or examination) was conducted must be viewed in light of the telephone conversations between the Division's auditor and petitioners' counsel. What emerges, at a minimum, is that documents were requested by, and at least some documents were furnished to, the Division. Offers to furnish additional documents, to "walk [the Division's auditor] through" those documents furnished, and an invitation to call if the Division's auditor "needed anything else and/or wanted any help in interpreting the documents he received," accompanied by a response that the Division's auditor would "be in touch when or if he needed anything," do not indicate or compel a conclusion that no audit review was conducted. To the contrary, it would appear that the Division's auditor concluded, upon the basis of reviewing the documents furnished and those otherwise available to the Division, and without resort to any additional information or assistance from petitioners' counsel, though offered, that there was a deficiency and that the issuance of the notices of deficiency was appropriate per Tax Law § 681(a). Whether the presentation of additional documents or other evidence might, as a matter of fact, overcome this conclusion remains a factual dispute thus leaving resolution via summary determination inappropriate. The extent of the Division's examination of information, including the documents apparently furnished by petitioners and information obtained by the Division independently (e.g., the Investment Proposals), appears to have fallen short of the extent of review desired by

petitioners or their counsel. However, this does not render the determination of deficiencies and the issuance of notices of deficiency based upon such an examination or review invalid.

D. As to the balance of petitioners' arguments, the existence (as admitted) of calculation errors in the dollar amount of the deficiencies asserted, such that the notices may be said to have been incorrect as inaccurate, does not render the same invalid, nor does correction of such calculation errors or further specification of the basis upon which the notices were issued establish that the Division lacked a rational basis for issuance of the notices or require the dismissal of such notices. (***see Matter of Tao v. New York State Tax Commn.***, 125 AD2d 879, 510 NYS2d 233 [1986], ***lv denied,*** 70 NY2d 601, 518 NYS2d 1023 [1987]). Notwithstanding petitioners' claim to the contrary, a reasonable reading of the notices bears out that at this stage of the proceedings there is no indication that petitioners were not and are not apprised of the existence of the asserted deficiencies, or of the basis upon which the deficiencies are asserted or the periods in question, or that petitioners have not been provided with sufficient information (including the ability to inquire and obtain additional information) so as to enable the preparation of a defense to the asserted deficiencies (***see Matter of Fillopow***, Tax Appeals Tribunal, June 16, 2009). Finally, no prejudice has been shown to have accrued against petitioners by virtue of the manner in which petitioners have received notice of the basis for and amount of the asserted deficiencies. (***Id., Matter of Tao v. New York State Tax Commn.***)

E. The petitioners' motion for summary determination is denied, and a hearing will be scheduled in due course.[2]

DATED: Troy, New York
July 16, 2009

/s/ Dennis M. Galliher
ADMINISTRATIVE LAW JUDGE

[2] To the extent the Division's filings in response to petitioners' motion for summary determination may be read to seek summary determination in the Division's favor, the same is denied upon the basis of the facts and conclusions set forth herein, noting in particular that there clearly exist unresolved issues of fact.