STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
JOSEPH LEE RICE, III FAMILY 1992 TRUST	:	DETERMINATION DTA NO. 822892
For Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law and the Administrative Code of the City of New York for the Years 1996 through 2000.	:	

Petitioner, Joseph Lee Rice, III Family 1992 Trust, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law and the Administrative Code of the City of New York for the Years 1996, 1997, 1998, 1999 and 2000.

On December 2, 2009 and December 7, 2009, respectively, petitioner, appearing by Hutton & Solomon LLP (Stephen L. Solomon, Esq., of counsel), and the Division of Taxation, appearing by Daniel Smirlock, Esq. (Kevin R. Law, Esq., of counsel), waived a hearing and submitted the matter for determination based on documents and briefs to be submitted by May 12, 2010, which date began the six-month period for issuance of this determination. After due consideration of the documents and arguments submitted, Joseph W. Pinto, Jr., Administrative Law Judge, renders the following determination.

ISSUE

Whether the Commissioner properly declined to exercise the discretionary refund authority contained in Tax Law § 697(d) and grant refunds that would otherwise be time-barred by the statute of limitations.

FINDINGS OF FACT

On October 27, 2009, the Division of Taxation (Division) and petitioner entered into a Stipulation of Facts, which contained 15 separately numbered paragraphs that have been incorporated into the facts below, except paragraphs 13, 14 and 15, which pertain to procedural matters that are not relevant or properly included in findings of fact.

1. By an agreement dated as of December 30, 1992, Joseph Lee Rice, III, as Settlor, created the Joseph Lee Rice, III Family Trust for the purposes therein stated. William B. Matteson, a partner in the New York City law firm of Debevoise & Plimpton LLP, was appointed Trustee and served as Trustee until his resignation on December 21, 2005.

2. At the time the Trust Agreement was originally drafted and executed, the Trustee, William B. Matteson, was domiciled in New York City. In 1995, the Trustee changed his domicile and place of residence to Vero Beach, Florida, while remaining of counsel with the law firm of Debevoise & Plimpton LLP.

3. For the tax years 1996 through 2003, petitioner filed New York fiduciary income tax returns (forms IT 205) as a resident trust reporting income, gains and losses from passive investments in securities and pass-through entities.

4. The fiduciary income tax returns for the tax years 1996 through 2003 were prepared by Richard Eisner & Co., LLP (now known as Eisner LLP) (Eisner), certified public accountants, located in New York City, and gave the address of the Trustee as being in care of Debevoise & Plimpton LLP, a New York City law firm that had represented the Settlor in drafting and implementing the Trust Agreement. The record did not disclose who supplied Eisner with the information necessary to prepare the fiduciary tax returns.

The fiduciary income tax return forms filed for all of the years in issue required the return preparer to provide the name, address and social security number of the trustee. In each year, it was provided at the top of the return and then again on a separate statement attached to the return. The latter was required by a specific question set forth in the return. For the years 1996, 1997, 1998 and 1999 it reported the trustee's address as "C/O Debevoise & Plimpton, 875 Third Avenue, New York, NY 10017" and that the trust was a full-year resident trust. For 2000, the address was changed to "C/O Debevoise & Plimpton, 919 Third Avenue, New York, NY 10022," indicating that a new address had been supplied to the tax return preparer.

5. The Trust filed the tax returns prepared by the accounting firm and paid the New York State and City fiduciary income tax shown due on such returns. The Trust Agreement provided that the Trustee could hire accountants to act in his behalf and delegate discretionary power to them (section 5.2[j]) and also the power to pay all taxes assessed against the Trust (section 5.2[q]).

6. Subsequently, it was brought to the return preparer's attention that the sole Trustee of the Trust for the years 1996 through 2003 was domiciled outside of New York. The record does not disclose who brought to Eisner's attention the Trustee's change of domicile.

7. Amended fiduciary income tax returns were filed for the tax years 1996 through 2003 that claimed refunds for the taxes paid for those years on the basis of the preparer's mistake as to the domicile of the Trustee when the original returns were filed.

8. The legal basis of the refund claims was that, pursuant to Tax Law § 605(b)(3)(D), no New York State or City income tax may be imposed on the Trust because:

(1) the trustee was domiciled outside New York State;

(2) the entire corpus of the Trust was located outside New York State; and

(3) all of the income and gains of the Trust were derived from or connected to sources outside New York State.

9. Refunds were issued for all taxes previously paid for the years 2001, 2002 and 2003; however, the refund claims for the years 1996, 1997, 1998, 1999 and 2000 were denied because they were filed outside the period of limitations for refund claims.

10. On June 8, 2006, petitioner's representative, Stephen L. Solomon, Esq., sent a letter to the former Commissioner of the Department of Taxation and Finance, Andrew Eristoff, requesting that the Commissioner use his special refund authority pursuant to Tax Law § 697(d) to grant the refunds requested for the years 1996 through 2000.

11. By letter dated October 18, 2006, Deborah R. Liebman, Deputy Counsel in the Office of Counsel, responded on behalf of the Commissioner and denied petitioner's request for the exercise of the special refund authority, noting that there was no mistake of fact that might have triggered the operation of the special refund authority provided for in Tax Law § 697(d). Further, Ms. Liebman noted that the error or errors must be clear from Department records, i.e., on the face of the returns filed, which was not the case in this matter.

CONCLUSIONS OF LAW

A. During 1992, the year the Joseph Lee Rice, III Family Trust was created, and at all pertinent times herein, Tax Law § 601(c) imposed an income tax on resident estates and trusts. However, for all years prior to January 1, 1996, the definition of a resident trust applicable to the Trust herein was contained in Tax Law § 605(b)(3)(C) as

> a trust, or portion of a trust, consisting of the property of:
>
> (i) a person domiciled in this state at the time such property was transferred to the trust, if such trust or portion of a trust was then irrevocable, or if it was then revocable and has not subsequently become irrevocable; or

> (ii) a person domiciled in this state at the time such trust, or portion of a trust, became irrevocable, if it was revocable when such property was transferred to the trust but has subsequently become irrevocable.

Since the Rice Trust was created and the property was transferred to the Trust by a New York domiciliary when this definition was in effect, the Rice Trust was a New York resident trust.

Tax Law § 605(b)(3) was amended by the Laws of 2003 (ch 658, § 1), effective for all tax years beginning on or after January 1, 1996, which included a new subparagraph (D) that reads as follows:

> (i) Provided, however, a resident trust is not subject to tax under this article if all of the following conditions are satisfied:
>
> (I) all the trustees are domiciled in a state other than New York;
>
> (II) the entire corpus of the trusts, including real and tangible property, is located outside the state of New York; and
>
> (III) all income and gains of the trust are derived from or connected with sources outside of the state of New York, determined as if the trust were a non-resident trust.

A similar provision was added to the Administrative Code of the City of New York which provided the following language:

> Provided, however, a resident trust is not subject to tax under this article if all of the following conditions are satisfied:
>
> (I) all the trustees are domiciled outside the city of New York . . . .

(Administrative Code of the City of New York 11-1705[b][3][D][i][I]; ***see also*** 20 NYCRR 105.23[c].)

Following the enactment of the amendment, on March 16, 2006, the Rice Trust filed amended fiduciary income tax returns for the years in issue, seeking refunds of tax paid with the original returns based on the 2003 amendment to Tax Law § 605(b)(3). The parties stipulated

that the entire corpus of the trust, including real and tangible property, was located outside the state of New York and that all income and gains of the trust were derived from or connected with sources outside of the state of New York, determined as if the trust were a nonresident trust. The central issue in this matter emanates from the first requirement, i.e., whether the trustee was domiciled in the City and State of New York. While the Division of Taxation agreed that petitioner had demonstrated that it had met all the requirements of Tax Law § 605(b)(3)(D) and granted the refunds requested for the years 2001, 2002 and 2003, it denied the refunds requested for 1996 through 2000 on the basis that the applications had been filed beyond the period of limitations on credits or refunds (Tax Law § 687[a]). Petitioner does not contend that it timely filed its refund claims for the years 1996 through 2000.

Although not articulated as a reason for creating an exception to the period of limitations on refunds set forth in Tax Law § 687(a), it should be noted that the amendment to Tax Law § 605(b)(3) in 2003 changed the definition of resident trust such that some taxpayers who had been considered residents were redefined as nonresidents as of January 1, 1996. However, the provision that tax years beginning on or after January 1, 1996 were subject to the terms of the amendment did not specifically modify the period of limitations set forth in Tax Law § 687(a) or create a new exception to its requirements. The reason for the law's application to tax years beginning on or after January 1, 1996 was specifically related to conforming the definition of resident with the Federal Riegle-Neal Interstate Banking and Branching Efficiency Act of 1996, which sought to encourage branch banking across state lines. The former definition of resident trust provided a chilling effect on New York banks that desired to convert out-of-state affiliates into branches, which might have subjected trusts established in and managed by the affiliate to

New York fiduciary income tax. (***See*** Memorandum in Support, S4703, Senator DeFrancisco, October 2, 2003.)[1]

B. Because petitioner recognized its inability to timely apply for the refunds consistent with Tax Law § 687(a), it appealed to the Commissioner of Taxation and Finance to exercise his discretionary power conferred by Tax Law § 697(d). That section provides as follows:

> Special refund authority. - - Where no questions of fact or law are involved and it appears from the records of the tax commission that any moneys have been erroneously or illegally collected from any taxpayer or other person, or paid by such taxpayer or other person under a mistake of facts, pursuant to the provisions of this article, the tax commission at any time, without regard to any period of limitations, shall have the power, upon making a record of its reasons therefor in writing, to cause such moneys so paid and being erroneously and illegally held to be refunded and to issue therefor its certificate to the comptroller.

In this instance, there is no contention that the Division erroneously or illegally collected monies from petitioner. Rather, the monies in question were voluntarily paid by petitioner upon filing the fiduciary income tax returns. Petitioner's contention is that it paid the taxes with its 1996 through 2000 returns under a mistake of fact, as opposed to a mistake of law.

In ***Matter of Wallace*** (Tax Appeals Tribunal, October 11, 2001) the Tax Appeals Tribunal adopted the following definitions in order to distinguish a mistake of law from a mistake of fact:

> A mistake of fact has been defined as an understanding of the facts in a manner different than they actually are (54 Am Jur 2d Mistake, Accident or Surprise § 4; ***see also***, ***Wendel Foundation v. Moredall Realty Corp***., 176 Misc 1006, 29 NYS2d 451). A mistake of law, on the other hand, has been defined as

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[1]The 2003 legislative amendment only codified what already existed in the Division's regulations at 20 NYCRR 105.23. In TSB-M-96(1)I, the Division stated that where the trustee is domiciled outside of New York, the corpus is located outside of New York and all income and gains are derived from sources outside of New York, no income tax can be imposed and the filing of a fiduciary income tax return is not required. The regulation was promulgated to comply with the decision in ***Matter of Mercantile-Safe Deposit and Trust Company v. Murphy*** (19 AD2d 765, 243 NYS2d 26 [1963], ***affd*** 15 NY2d 579, 255 NYS2d 96 [1964] [wherein the court held that New York lacked jurisdiction to tax income accumulated in a trust established by a New York resident where the trust was administered, the corpus was located, and the trustee was domiciled in Maryland). Therefore, the definition of resident trust set forth in the 2003 amendment to Tax Law § 605(b)(3) was virtually the same as that which was in contained in the Division's regulations during the period in issue.

> acquaintance with the existence or nonexistence of facts, but ignorance of the legal consequences following from the facts (54 Am Jur 2d Mistake, Accident or Surprise § 8; ***see also, Wendel Foundation v. Moredall Realty Corp.***, ***supra***).

C. Petitioner contends that the tax return preparer, Richard Eisner & Co., LLP, made a mistake as to the domicile of the Trustee, Mr. Matteson, and that this was a mistake of fact, which was contemplated by the definition in ***Matter of Wallace***.

The Division of Taxation countered this argument by pointing out that the Trustee signed all the original fiduciary returns for the years in issue, each of which stated his New York address in care of Debevoise & Plimpton, 875 Third Avenue (919 Third Avenue in 2000), New York, New York. Thus, the Division contends that the Trustee knowingly continued to state a New York address, which information was within his personal knowledge and which he knew or should have known would be relied upon by others who viewed the return.

First, it must be noted that the Trust document itself states on its first page that both the settlor, Mr. Rice, and the Trustee, Mr. Matteson, were both "of New York, New York" as of December 30, 1992, i.e., they were New York domiciliaries. Not until Mr. Matteson's resignation in December 2005 was his out-of-state address disclosed in documents contained in the record, notwithstanding the stipulated finding. Further, it was Mr. Matteson who voluntarily chose to use his law firm's address and not his personal residence or some other address. As the Division pointed out, it is reasonable to assume that Mr. Matteson knew his own domicile at all times pertinent herein and that a New York resident fiduciary income tax return was being filed for each of the years in issue that clearly stated his name and New York address in care of his law firm.

The fiduciary income tax return forms filed for all of the years in issue required the return preparer to provide the name, address and social security number of the trustee. In each year, it

was provided on a separate statement attached to the return. For the years 1996, 1997, 1998 and 1999 it reported the trustee's address as "C/O Debevoise & Plimpton, 875 Third Avenue, New York, NY 10017" and that the trust was a full-year resident trust. For 2000, the address was changed to "C/O Debevoise & Plimpton, 919 Third Avenue, New York, NY 10022," indicating that a new address had been supplied to the tax return preparer. Since the record is devoid of any evidence regarding how the tax preparer acquired its information to prepare the return and whether it was aware of the Division's regulations concerning resident trusts (***see*** footnote 1 above), it is impossible to conclude that it relied on a mistake of fact concerning the Trustee's address. One would be equally justified in concluding that the tax preparer (or the Trustee) had made a mistake of law based upon the pattern of reporting that presents itself for the years in issue, particularly after reporting the change of address in 2000.

To suggest that the tax return preparer mistook the domicile of the Trustee when it was specifically stated on the first page of the return and then again in a separate statement attached to each return is untenable. This information was confirmed, or should have been confirmed, each year when Eisner was provided the information for preparation of the returns and when the Trustee reviewed and signed the returns. More importantly, however, the tax return preparer was merely the agent of Mr. Matteson, hired to prepare returns based on information it received from the Trustee.[2] Any fact relied upon by Eisner that may have been incorrect or mistaken was provided or confirmed by Mr. Matteson, who provided or confirmed the information as fiduciary for the Trust. As such, it cannot be said that either Eisner or the Trustee prepared and signed the returns under a mistake of fact.

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[2]The Trust Agreement specifically granted to Mr. Matteson, Trustee, the power to appoint and compensate agents, including accountants, to act on the Trustee's behalf. (Trust Agreement § 5.2[j].) It also conferred on the Trustee alone the power to pay all taxes assessed against the Trust (Trust Agreement § 5.2[q]).

The June 8, 2006 letter from Stephen L. Solomon to Commissioner Eristoff argues that the return preparer relied on the address provided by the Trustee since the inception of the Trust in 1992, and made the assumption that the Trustee had remained domiciled in New York throughout the years in issue. Thus, he concluded that the return preparer had operated under a mistake of fact. However, as discussed above, the address was changed once during the period in issue and each year the return required a statement of the Trustee's address and social security number. Both the Trustee, who knew his own domicile, and return preparer, who relied on the Trustee for information needed to complete the return, had an annual opportunity (and an obligation of due diligence) to change the address but did not. Under these circumstances, neither the Trustee's nor his agent's reliance on information within the personal knowledge of the Trustee can be characterized as a mistake of fact.

D. Petitioner's reliance upon ***Matter of Berry*** (Tax Appeals Tribunal, January 22, 2004) is misplaced. There an accountant was held to have made a mistake of law and did not have a different understanding of the facts than what they actually were. Petitioner takes this holding to indicate that if the accountant had operated under a mistake of fact, it would have permitted the Commissioner to use his discretionary special refund authority. However, since it has been concluded that Eisner had all the information that was provided by its principal, the Trustee, it was not operating under a mistake of fact. Mr. Matteson knew his own domicile during each of the years in issue and, for some unknown reason, provided the address of Debevoise & Plimpton in New York City. It can only be speculated that he was unaware of the New York regulation at 20 NYCRR 105.23 and the tax ramifications of his out-of-state domicile - - a mistake of law.

Likewise, petitioner's reliance on ***Matter of Mobil Oil Corporation v. Commissioner of Finance*** (101 AD2d 723, 475 NYS2d 32 [1984]) was misplaced. There the issue was not

whether there was a payment made under a mistake of fact, but the simple failure to timely apply for a refund. The Court was disturbed by the Commissioner's ability to pursue a tax deficiency reassessment when a taxpayer could not claim a refund for the same tax year, where there had been a change in a taxpayer's income or capital gain. Under these circumstances the Court believed it was incumbent upon the Commissioner to use his discretionary refund authority to remedy the inequity.

E. The petition of Joseph Lee Rice, III Family 1992 Trust is denied and the five notices of disallowance, dated February 16, 2007, are sustained.

DATED: Troy, New York
November 4, 2010

/s/ Joseph W. Pinto, Jr.
ADMINISTRATIVE LAW JUDGE