

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions	:	
of	:	
ROBERT AND KIRA CIARDULLO	:	DETERMINATION
for the Redetermination of Deficiencies or for Refund	:	DTA NOS. 828251,
of New York State Personal Income Tax	:	829356, 829357,
under Article 22 of the Tax Law for the Years	:	829671 AND 829938
2012, 2013, 2014, 2015, and 2016.	:	

Petitioners, Robert and Kira Ciardullo, filed petitions for redetermination of deficiencies or for refund of New York State personal income tax under article 22 of the Tax Law for the years 2012, 2013, 2014, 2015, and 2016.

On October 21, 2020, the Division of Taxation, appearing by Amanda Hiller, Esq. (Peter B. Ostwald, Esq., of counsel), and on October 30, 2020, petitioners, appearing by Benjamin R. Katz, Esq., waived a hearing and submitted the matter for a determination based on documents and briefs to be submitted by May 12, 2021, which date began the six-month period for issuance of this determination. After due consideration of the documents and arguments submitted, Barbara J. Russo, Administrative Law Judge, renders the following determination.

ISSUES

I. Whether, for purposes of the add-back to federal adjusted gross income under Tax Law § 612 (b) (1), interest income paid on bonds issued by states other than New York, which are federally tax-exempt but taxable in New York, equals either the gross interest income paid on the bonds, or such gross interest paid less amortized bond premiums allocable to the tax year.

II. Whether petitioner Robert Ciardullo was engaged in a trade or business as a bond

trader.

III. Whether the taxation of gross interest income paid on bonds issued by states other than New York violates the New York or United States Constitutions.

FINDINGS OF FACT

1. During the years 2012 through 2016 (the years at issue), petitioners, Robert and Kira Ciardullo, were residents of New York State.

2. For the years at issue, petitioners engaged in various investing activities. As part of their overall investing strategy, petitioners bought and held federally tax-exempt obligations issued by state and local governments other than New York (municipal bonds or bonds). In some instances, petitioners paid a premium to acquire the bonds.

2012

3. Petitioners timely filed a New York resident income tax return for 2012 on April 15, 2013 (2012 initial return). On the 2012 initial return, petitioners reported federal adjusted gross income of \$1,452,750.00 consisting of wages, salaries and tips of \$1,146,885.00,¹ taxable interest income of \$268.00, ordinary dividends of \$1,677.00, business income of \$9,299.00,² a capital loss of \$119.00,³ rental real estate, royalties, partnerships and S corporation income of \$296,576.00, and a federal adjustment of \$1,836.00. On line 20 of the 2012 initial return, petitioners reported a New York addition for interest income on non-New York state and local bonds and obligations of \$183,596.00, and on line 23 included a New York addition for “other” in the amount of \$164.00. Petitioners claimed an itemized deduction of \$72,002.00, and reported taxable income of \$1,564,508.00, New York State tax of \$107,169.00, tax withheld of

¹ Attached to the 2012 initial return is form W-2, wage and tax statement for Robert Ciardullo from Robert C. Ciardulo MD PC showing wages of \$1,047,978.11. There was no explanation for the discrepancy.

² A 2012 schedule C, profit or loss from business, reports the business income for Kira Geraci-Ciardullo MD, as medical doctor: allergist.

\$96,439.00, and tax due of \$10,730.00.

4. On April 15, 2015, petitioners filed an amended resident income tax return, form IT-201-X, for 2012 (first 2012 amended return). On the first 2012 amended return, petitioners amended line 20, New York additions for interest income on non-New York state and local bonds and obligations, to \$32,839.00. Petitioners reported New York adjusted gross income of \$1,485,753.00, claimed a standard deduction of \$15,000.00, reported taxable income of \$1,470,753.00, and tax of \$100,747.00. Petitioners reported total payments of \$111,451.00, consisting of tax withheld of \$96,439.00 and amount paid with original return of \$15,012.00, and requested a refund of \$10,704.00. Petitioners reported Robert Ciardullo's occupation as "Medical Doctor Surgeon" on the first 2012 amended return.

5. On July 6, 2015, the Division of Taxation (Division) issued an account adjustment notice to petitioners for 2012 in response to their first 2012 amended return. The account adjustment notice adjusted total payments to \$107,169.00, adjusted the refund to \$6,701.35, and issued a refund check to petitioners in that amount for 2012.

6. On November 30, 2015 the Division issued to petitioners a statement of proposed audit changes (2012 statement) for the year 2012, stating in part:

"Interest income on obligations from any state other than New York State or any political subdivision of another state, though exempt from federal income tax, is taxable to New York (Sections 612 (b) (1) and 1303 of the New York State Tax Law). Such income should have been reported on line 20 of the 2012 Form IT-201.

All or part of the income that was credited to your account or which you received from the mutual fund(s) shown below was derived from non-New York State and local obligations. Because you did not make the proper line modification on your New York State return, we have adjusted your New York taxable income for the portion of the non-New York interest income included in your distribution(s) from the mutual fund(s). . . ."

The 2012 statement listed taxable amounts from several mutual fund distributions of

³ Petitioners' 2012 schedule D, capital gains and losses, reports a long-term capital loss of \$119.00.

non-New York interest made to petitioners totaling \$178,585.00, less the amount reported on petitioners' return of \$32,839.00, for a net adjustment of \$145,746.00. The statement further explained:

“Many bond funds invest in obligations of both non-New York and New York securities. Interest income generated from a New York State or municipal bond security is not taxable. For any bonds earning interest from New York State or municipal sources, that portion has been eliminated in the computation of your taxable interest income.

The information we have concerning the amount of state and local bond interest that you earned was obtained from your payer. Payers are required to report this data under Section 658 of the New York State Tax Law. If you cannot reconcile this information with what was reported to you by your payer(s) or broker(s) on your 2012 year-end statements, you must contact your broker(s) for an explanation. We cannot adjust our billing without a statement from your payer(s) identifying the amount, the fund, account number, cusip number and the percentage of each fund's portfolio that represents non-New York bond interest.”

The 2012 statement recalculated petitioners' New York adjusted gross income to \$1,631,499.00, determined taxable income of \$1,616,499.00 and tax of \$110,730.00, and asserted additional tax due of \$9,983.00 plus interest.

7. The Division issued to petitioners a notice of deficiency, assessment number L-044051602, dated April 4, 2016, asserting tax due of \$9,983.00 plus interest for tax year 2012.

8. On April 5, 2016, petitioners filed a second amended resident income tax return, form IT-201-X, for 2012 (second 2012 amended return). On the second 2012 amended return, petitioners again amended line 20, New York additions for interest income on non-New York state and local bonds and obligations, to \$202,286.00. Petitioners amended line 31 for New York subtractions, reporting as “other” “accrued interest on bonds” in the amount of \$48,495.00. Petitioners reported New York adjusted gross income of \$1,606,541.00. Petitioners also amended their deductions, claiming itemized deductions of \$233,981.00. Petitioners reported taxable income of \$1,372,560.00 and tax of \$94,020.00. Petitioners reported total payments of \$111,451.00, consisting of tax withheld of \$96,439.00 and amount paid with original return of

\$15,012.00, and requested a refund of \$8,736.00. Petitioners reported Robert Ciardullo's occupation as Doctor on the second 2012 amended return.

9. On April 12, 2016, the Division sent a response to petitioners' inquiry regarding assessment number L-044051602 for 2012, stating in part:

"The information we have concerning the amount of state and local bond interest that you earned was obtained from your payer. Payers are required to report this data under New York Tax Law, section 658. If you cannot reconcile this information with what was reported to you by your payer(s) or broker(s) on your 2012 year-end statements, you must contact your broker(s) for an explanation.

We cannot adjust our billing without a statement from your payer(s) identifying the amount, the fund, account number, CUSIP number, and the percentage of each fund's portfolio that represents non-New York bond interest."

10. On April 16, 2016, petitioners filed a third amended resident income tax return, form IT-201-X, for 2012 (third 2012 amended return). On the third 2012 amended return, petitioners again amended line 20, New York additions for interest income on non-New York state and local bonds and obligations, to (- \$3,806.00). Next to the line for New York additions, petitioners wrote "see attached." Petitioners attached to the third 2012 amended return a schedule entitled "Schedule of Actual Interest Earned Net of Deduction of Non NYS Exempt Bond Interest Premium and Accrued Interest on Non-NYS Exempt Bond Interest For Year 2012 Form 201X Line 20: 'Additions.'" Petitioners listed the following on the schedule:

"Total NYS Tax Exempt Interest Per NYS Audit Number X922844839	178585
Less Accrued Interest Per Confirmations Previously Sent	- 48,495
Less Bond Premium Offset Per Schedule	<u>-133896</u>
<u>Additions Per Line 20 IT 201X Year 2012</u>	<u>- 3806"</u>

Petitioners left line 31, other New York subtractions, blank on the third 2012 amended return. Petitioners reported New York adjusted gross income of \$1,448,944.00, claimed a

standard deduction of \$15,000.00, reported taxable income of \$1,433,944.00, and tax of \$98,225.00. Petitioners reported total payments of \$111,451.00, consisting of tax withheld of \$96,439.00 and amount paid with original return of \$15,012.00, and requested a refund of \$2,531.00.

11. On May 2, 2016, the Division sent another response to petitioners' inquiry regarding assessment number L-044051602 for 2012, stating in part:

“We have reviewed your Confirmations and calculated \$45,984.00 of accrued interest expenses related to bonds specifically listed in our 2012 assessment. We are unable to include accrued interest from 2010.

Based on the documentation you submitted, we have reduced the taxable municipal bond interest on Line 20 of form IT-201, from \$178,585.00 (reported by Pershing, LLC) to \$132,601.00.

Please be advised that bond premium amortization is not a direct offset to taxable municipal bond interest earned, but rather an itemized deduction addition to be reported on Line 11 of the New York State itemized deduction worksheet.

Since you claimed the appropriate New York State standard deduction for the 2012 tax year, no adjustment can be made to this assessment based on the eligible amortization amounts identified in your correspondence.

We are unable to offset bond interest with amortization based on your claim that you are an investor/trader, since this activity must be attributable to a trade or business carried on by the taxpayer (see New York State Tax Law section 612(c)(10)).

Based on our adjustments, your return has been recomputed.

Line 019 Federal Adjusted Gross Income	1,452,750.00	
Line 020 Interest Income on State/Local Bonds	132,601.00	
Line 033 New York Adjusted Gross Income	1,585,515.00	
Line 34 New York Deductions	15,000.00	
Line 37 New York Taxable Income	1,570,515.00	
Line 061 Total Tax and Contributions	107,580.28	
	NY State	(=) Total
Revised Total Tax	107,580.28	107,580.28
Tax Previously Stated (-)	100,747.00	100,747.00
Net Tax Due (=)	6,833.28	6,833.28

The tax due has been adjusted based on the additional information you supplied.”

12. On August 30, 2016, the Division sent another response to petitioners' inquiry

regarding assessment number L-044051602 for 2012, stating in part:

“We received your reply and revised information about the above assessment(s).

This bill is determined to be correct for the reasons which were previously explained to you in our Adjustment Notice dated 05/02/16.

Trading for your own personal account is investing, not a trade or business.

Interest income from state or local bonds, other than New York, are taxable to a New York State resident under section 612(b)(1) and 1303 of the New York State Tax Law.

If you buy a bond between interest payment dates, part of the purchase price of that bond represents interest accrued before the date of purchase. If you receive a statement from your broker which reflects the full amount of interest, which includes the accrued amount, you are entitled to net the accrued interest against that amount reported via your broker's statement in reporting the appropriate addition modification.

Based on the information submitted we have allowed the deduction of accrued interest paid in the amount of \$45,984.00 from the interest income earned on Non New York State and local bonds for only the bonds listed on our bill.

If you purchase a non New York State or local bond at a premium, the amortized portion of the premium paid may only be deducted as an itemized deduction. You cannot net the amortized portion of the bond premium against the bond interest that you are reporting as an addition modification. The only exception is if the bond is used in a trade or business. In that instance the premium can be deducted as an above the line deduction.

Your representative indicated in his letter dated 05/06/16 that you are entitled to subtracted bond premium amortization from the non NY bond interest you earned at line 20 of your 2012 income tax return.

Please note bond premium amortization cannot be directly subtracted from your interest income.

The bond premium amortization should be reported as an addition adjustment at line 11 on form IT-201-D, New York State Resident Itemized Deduction Schedule.

Therefore, the bond premium amortization you subtracted from the bond interest you earned reported at line 20 of your 2012 amended income tax return has been disallowed.

Our records indicate that you were allowed the standard deduction and therefore, the bond premium amortization is not allowed.”

The correspondence showed tax due of \$6,833.28 plus interest for the year 2012.

13. On August 31, 2016, the Division issued a notice of disallowance to petitioners disallowing their claim for refund of \$2,531.00 for 2012, stating, in part:

“2012 Bill #L044051602 dated 11/30/15 is determined to be correct for the reasons which were previously explained to you in our Adjustment Notice dated 05/02/16. Therefore, the refund claimed on your 2012 amended return dated 04/15/16 is disallowed.”

The notice of disallowance further contained the same explanation as that in the August 30, 2016 correspondence (*see* finding of fact 12).

14. On September 23, 2016, the Division issued to petitioners a notice and demand for payment of tax due for assessment number L-044051602 for tax year 2012, asserting tax due of \$6,833.28 plus interest.

15. Petitioners reported Robert Ciardullo’s occupation as Doctor on his 2012 federal form 1040, U.S. individual income tax return.

16. Petitioners submitted into the record 2012 Tax and Year-End Statements from Cetera Advisors LLC. The 2012 year-end statement for Robert Ciardullo shows federally tax-exempt interest income of \$159,307.52, specified private activity bond interest of \$5,500.00, ordinary dividends of \$14.87, accrued interest purchased of \$38,236.17, and proceeds from broker and barter exchange transactions of (\$118.96). The proceeds from broker and barter exchange transactions consisted of two long-term transactions of securities acquired on June 30, 2010 and sold on December 3, 2012, and securities acquired on December 10, 2008 and sold on January 3, 2012, for a net loss of \$118.97, and a short-term transaction of securities acquired on February 9, 2012 and sold on December 3, 2012 for a gain of \$.01.

The 2012 year-end statement for Kira Ciardullo shows federally tax-exempt interest income of \$47,288.75, specified private activity bond interest of \$1,375.00, ordinary dividends of \$37.56, and accrued interest purchases of \$22,278.60. The 2012 form 1099-B, proceeds from broker and barter exchange transactions, included with the year-end statement, shows a

redemption of securities for which short or long-term determination was unknown to the broker, with a realized gain or loss of \$0.00.

2013

17. Petitioners filed a New York resident income tax return for 2013 on November 3, 2014 (2013 initial return). On the 2013 initial return, petitioners reported federal adjusted gross income of \$991,229.00 consisting of wages, salaries and tips of \$879,532.00,⁴ taxable interest income of \$1,797.00, ordinary dividends of \$175.00, business income of \$1,126.00,⁵ no capital gain or loss, rental real estate, royalties, partnerships and S corporation income of \$108,614.00, and a federal adjustment of \$15.00. On line 20 of the 2013 initial return, petitioners reported a New York addition for interest income on non-New York state and local bonds and obligations of \$43,521.00. Petitioners reported New York adjusted gross income of \$1,034,750.00, claimed a standard deduction of \$15,400.00, and reported taxable income of \$1,019,350.00, New York State tax of \$69,825.00, tax withheld of \$87,733.00, and requested a refund of \$17,908.00. The 2013 initial return lists Robert Ciardullo's occupation as plastic surgeon.

18. On November 26, 2014, the Division issued a refund check to petitioners in the amount of \$17,908.00 for tax year 2013.

19. On December 30, 2016, the Division issued to petitioners a statement of proposed audit changes, assessment number L-045883894, for the year 2013 (2013 statement), stating that “[t]he interest income on state and local bonds and obligations shown on your return does not agree with the amount(s) reported by the payer(s).” The 2013 statement further explained:

“The following income is taxable to New York (NYS Tax Law sections 612(b)(1)

⁴ Attached to petitioners' initial 2013 return are forms W-2, wage and tax statements for Robert Ciardullo from Robert C. Ciardulo MD PC showing wages of \$739,231.75 and for Kira Ciardullo from Westchester Health Associates, PLLC, showing wages of \$140,300.00.

⁵ A 2013 schedule C-EZ, net profit or loss from business, reports the business income for Kira Geraci-Ciardullo MD, as medical doctor: allergist.

and 1303):

- Interest income on obligations from any state other than New York State or any political subdivision of another state;
- Interest or dividend income on obligations or securities of any authority, commission, or instrumentality of the United States, which the laws of the United States exempt from federal income tax but not from state income taxes.

You must report such income on line 20 of your 2013 personal income tax return.

All or part of the income that was credited to your account or which you received from the sources shown in the Fund details section of this notice was derived from non-New York State and local obligations. Because you did not make the proper line modification on your New York State return, we adjusted your New York taxable income for the portion of non-New York interest income included in your distributions from these sources.”

The 2013 statement listed taxable amounts from several fund distributions of non-New York interest income made to petitioners totaling \$337,035.00, less the amount reported on petitioners’ return of \$43,521.00, for a net adjustment of \$293,514.00. The statement further explained:

“Many funds invest in obligations of both non-New York and New York securities. Interest income generated from a New York State or municipal bond security is not taxable. We did not include investment interest from New York State or municipal sources when we computed your taxable income.

We obtained the information we have concerning the amount of state and local bond interest that you earned from your payer. Payers are required to report this data under NYS Tax Law, section 658. If you cannot reconcile this information with what your payer or broker reported to you on your 2013 year-end statements, you must contact your payer or broker for an explanation. We cannot adjust our billing without a statement from your payer or broker”

The 2013 statement recalculated petitioners’ New York adjusted gross income to \$1,328,264.00, determined taxable income of \$1,312,864.00 and tax of \$89,931.00, and asserted tax due of \$20,106.00 plus interest.

20. On August 7, 2017, the Division sent a notice of assessment resolution to petitioners regarding assessment number L-045883894 for the year 2013, stating, “Based on our review of the information provided, the assessment(s) is sustained and your request for refund or credit is

denied.” The notice of assessment resolution shows tax due of \$20,106.00 plus interest, and payments/credits of \$23,727.10, with no balance due.⁶

21. On September 15, 2017, petitioners filed an amended resident income tax return, form IT-201-X, for 2013 (2013 amended return). On the 2013 amended return, petitioners amended line 20, New York additions for interest income on non-New York state and local bonds and obligations, to \$33,026.00. Petitioners amended line 31 for New York subtractions, reporting as “other” “accrued interest” in the amount of \$22,012.00. Petitioners reported New York adjusted gross income of \$1,002,243.00. Petitioners also amended their deductions, claiming itemized deductions of \$7,300.00. Petitioners reported taxable income of \$994,943.00 and tax of \$68,154.00. Petitioners reported total payments of \$107,839.00, consisting of tax withheld of \$87,733.00 and amount paid with original return of \$20,106.00, and reported a refund due of \$21,777.00. Petitioners reported Robert Ciardullo’s occupation as Doctor on the 2013 amended return.

22. Petitioners attached to the 2013 amended return a “disclosure statement for refund claim due to appeal of disallowance of amortized premium and other adjustments” in which they stated they will appeal the assessment and have paid under protest the assessment for 2013, and requested that a refund check not be sent until the matter is resolved at a conciliation conference or subsequent appeal.

23. Also attached to the 2013 amended return was a “schedule of interest additions for municipal bonds other than New York State” with reference to line 20 of the return, on which petitioners list “qualified stated interest on municipal bonds other than New York State” of \$337,035.00 less “amortized premium” of \$304,009.00, totaling “interest additions for municipal

⁶ A case contact in the Division’s audit file for 2013 indicates that the 2013 assessment was paid in full before a notice of deficiency was issued.

bonds other than New York State” of \$33,026.00.

24. On May 30, 2019, the Division issued to petitioners a notice of disallowance for 2013, sustaining assessment number L-045883894 which had been paid in full, and denying the refund claim of \$21,777.00. The notice of disallowance for 2013 states, “Bond premium amortization expenses are not a direct offset to taxable municipal bond interest earned, but rather an itemized deduction addition to be reported on Line 11 – Addition adjustments of the IT-201-D Resident Itemized Deduction Schedule.”

25. Petitioners submitted into the record portions of 2013 Tax and Year-End Statements from Cetera Advisors LLC. The 2013 year-end statement for Robert Ciardullo shows federally tax-exempt interest income of \$229,802.56 and specified private activity bond interest of \$12,575.00. The first page of the statement also shows a summary of form 1099-B with gross proceeds of \$110,000.00 and a cost basis of \$0.00, and refers to the 1099-B section of the statement for details. However, pages 2 through 4 of the 2013 year-end statement were not submitted by petitioners and the documents submitted do not contain the 1099-B section detail.

The 2013 year-end statement for Kira Ciardullo shows federally tax-exempt interest income of \$122,278.81 and specified private activity bond interest of \$1,375.00.

2014

26. Petitioners filed a New York resident income tax return for 2014 on October 14, 2015 (2014 initial return). On the 2014 initial return, petitioners reported federal adjusted gross income of \$1,245,372.00 consisting of wages, salaries and tips of \$991,842.00,⁷ taxable interest income of \$214.00, ordinary dividends of \$5,453.00, taxable refunds, credits or offsets of state

⁷ Attached to petitioners’ initial 2014 return are forms W-2, wage and tax statements for Robert Ciardullo showing wages of \$852,440.42, with the section for employer’s name and address left blank, and for Kira Ciardullo from Westchester Health Associates, PLLC, showing wages of \$139,402.00.

and local income taxes of \$17,908.00, business income of \$1,506.00,⁸ capital gains of \$6,845.00,⁹ rental real estate, royalties, partnerships and S corporation income of \$221,624.00, and a federal adjustment of \$20.00. On line 20 of the 2014 initial return, petitioners reported a New York addition for interest income on non-New York state and local bonds and obligations of \$67,710.00. On line 25, for New York subtractions, petitioners subtracted \$17,908.00 for taxable refunds, credits, or offsets of state and local income taxes. Petitioners reported New York adjusted gross income of \$1,295,174.00, claimed a standard deduction of \$15,650.00, and reported taxable income of \$1,279,524.00, New York State tax of \$87,647.00, tax withheld of \$94,094.00, and requested a refund of \$6,447.00. The 2014 initial return lists Robert Ciardullo's occupation as plastic surgeon.

27. On November 17, 2015, the Division issued a refund check to petitioners in the amount of \$6,447.00 for tax year 2014.

28. On January 22, 2018, the Division issued to petitioners a statement of proposed audit changes, assessment number L-047622663, for the year 2014 (2014 statement), stating that “[t]he interest income on state and local bonds and obligations shown on your return does not agree with the amount(s) reported by the payer(s).” The 2014 statement generally contained the same explanation as the 2013 statement (*see* finding of fact 19), and indicated the petitioners were required to report the interest income from non-New York sources on line 20 of the 2014 return.

The 2014 statement listed taxable amounts from several fund distributions of non-New York interest made to petitioners totaling \$352,529.39, less the amount reported on petitioners'

⁸ A 2014 schedule C, profit or loss from business, reports the business income for Kira Geraci-Ciardullo MD, as medical doctor: allergist.

⁹ Petitioners' 2014 schedule D, capital gains and losses, reports a short-term capital gain of \$25.63 for an equity dividend fund held for four months, and long-term capital gains of \$6,819.00 for assets held for over one year.

return of \$67,710.00, for a net adjustment of \$284,819.39. The 2014 statement noted that the Division's computation of taxable income did not include interest from New York State or municipal sources.

The 2014 statement recalculated petitioners' New York adjusted gross income to \$1,579,993.00, determined taxable income of \$1,564,343.00 and tax of \$107,157.00, and asserted tax due of \$19,510.00 plus interest.

29. On April 17, 2018, petitioners filed an amended resident income tax return, form IT-201-X, for 2014 (2014 amended return). On the 2014 amended return, petitioners amended their deductions from standard to itemized deductions of \$9,822.00. Petitioners reported taxable income of \$1,285,352.00 and tax of \$88,047.00. Petitioners reported total payments of \$107,157.00, consisting of tax withheld of \$94,094.00 and amount paid with original return of \$13,063.00, and reported an overpayment of \$19,110.00. Petitioners included with the 2014 amended return an attached statement stating that "the Taxpayers are protesting and appealing the 1/22/2018 Statement of Proposed Audit Change, Assessment ID: L-047622663-3. Please do not refund any money at this time."

30. On June 4, 2018, the Division sent to petitioners a notice of assessment resolution regarding assessment number L-047622663, for the year 2014. The notice of assessment resolution states:

"We have received the IT-201-X Amended Resident Income Tax Return filed as a protest to the above NYS assessment L-047622663-3 (2014). The IT-201-X (2014) has not been accepted and processed by our department.

Thank you for your payment of \$23,132.81 on February 14, 2018 which has paid the above assessment in full.

We have reviewed the information you sent in response to the above assessment. The assessment L-047622663-3 (2014) is considered correct as issued and has been sustained.

The assessment is determined to be correct as issued for the following reasons

which were previously explained to you in notices sent by our department.

Please note bond premium amortization cannot be directly subtracted from your interest income. The following court rulings support our department's treatment of amortization:

- Advisory Opinion TSB-A-03(3)I – George Lavenia
- Tribunal Decision DTA No. 822845, Howard Solomon, dated June 2, 2011
- ALJ (Administrative Law Judge) Determination DTA NO. 826159, Steve Kanney, dated September 3, 2015

The only exception is if the bond is used in a trade or business. In that instance the bond premium amortization can be deducted as an above the line deduction. Trading for your own account is investing, not a trade or business.

The bond premium amortization should be reported as an addition adjustment on line 11 of Form IT-201-D, New York State Resident Itemized Deduction Schedule.

If you paid accrued interest on the purchase of municipal bonds provide our department the 2014 year-end statements from Pershing LLC that itemizes the accrued interest paid by CUSIP number and security description, and your case will be reviewed again.”

The notice of assessment resolution shows tax assessed for 2014 of \$19,510.00 plus interest of \$3,622.81, less payments/credits of \$23,132.81, and no current balance.

31. On May 30, 2019, the Division issued to petitioners a notice of disallowance for 2014, sustaining assessment number L-047622663 which had been paid in full, and denying the refund claim of \$12,663.00. The notice of disallowance for 2014 states, “Bond premium amortization expenses are not a direct offset to taxable municipal bond interest earned, but rather an itemized deduction addition to be reported on Line 11 – Addition adjustments of the IT-201-D Resident Itemized Deduction Schedule.”

32. Petitioners submitted into the record portions of 2014 Tax and Year-End Statements from Cetera Advisors LLC. The 2014 year-end statement for Robert Ciardullo shows federally tax-exempt interest income of \$222,896.30, specified private activity bond interest of \$12,575.00, ordinary dividends of \$2.18, exempt interest dividends of \$20,356.78, and specified private activity bond interest dividends of \$4,010.06. The first page of the statement also shows

a summary of form 1099-B with gross proceeds of \$677,437.60 and a cost basis of \$0.00, and refers to the 1099-B section of the statement for details. However, pages 2 through 6 of the 2014 year-end statement were not submitted by petitioners and the documents submitted do not contain the 1099-B section detail.

The 2014 year-end statement for Kira Ciardullo shows federally tax-exempt interest income of \$122,516.31 and specified private activity bond interest of \$1,375.00. Line 11 of the 2014 1099-INT, interest income, shows bond premium for covered transactions of \$340.37. The 2014 statement shows ordinary dividends of \$0.60, exempt interest dividends of \$7,508.69, and specified private activity bond interest dividends of \$1,609.99. The first page of the statement also shows a summary of form 1099-B with gross proceeds of \$285,000.00 and a cost basis of \$0.00, and refers to the 1099-B section of the statement for details. However, pages 2 through 4 of the 2014 year-end statement were not submitted by petitioners and the documents submitted do not contain the 1099-B section detail.

2015

33. Petitioners filed a New York resident income tax return for 2015 on July 15, 2016 (2015 initial return). On the 2015 initial return, petitioners reported federal adjusted gross income of \$1,113,942.00 consisting of wages, salaries and tips of \$930,245.00,¹⁰ taxable interest income of \$491.00, ordinary dividends of \$6,581.00, taxable refunds, credits or offsets of state and local income taxes of \$21,495.00, business loss of \$7,993.00,¹¹ capital loss of \$695.00,¹²

¹⁰ Attached to petitioners' initial 2015 return are forms W-2, wage and tax statements for Robert Ciardullo showing wages of \$857,233.26 from Robert C. Ciardulo MD PC, and for Kira Ciardullo from Westchester Health Associates, PLLC, showing wages of \$73,022.28.

¹¹ A 2015 schedule C, profit or loss from business, reports the business loss for Kira Geraci-Ciardullo MD, as medical doctor.

¹² Petitioners' 2015 schedule D, capital gains and losses, reports a long-term capital loss of \$695.00 for assets held for over one year.

and rental real estate, royalties, partnerships and S corporation income of \$163,318.00. On line 20 of the 2015 initial return, petitioners reported a New York addition for interest income on non-New York state and local bonds and obligations of \$300,685.00. On line 23 for “other” New York additions petitioners reported \$300,685.00 and attached form IT-225, other additions and subtractions statement, indicating in part 1, other New York additions, interest expense on loans used to buy obligations exempt from New York State tax and other expenses relating to the production of income exempt from New York State tax of \$300,685.00.

On line 25, for New York subtractions, petitioners subtracted \$21,495.00 for taxable refunds, credits, or offsets of state and local income taxes. On line 31, for “other” New York subtractions, petitioners reported \$210,580.00 and indicated on a statement attached to form IT-225 subtractions for amortization of premium non-NYS bonds of \$190,409.49 and accrued interest paid on non-NYS bonds of \$20,170.24.

Petitioners reported New York adjusted gross income of \$1,182,552.00, claimed a standard deduction of \$15,850.00, and reported taxable income of \$1,166,702.00, New York State tax of \$79,919.00, tax withheld of \$94,015.00, and requested that an overpayment of \$14,096.00 be applied to the following year’s estimated tax. The 2015 initial return lists Robert Ciardullo’s occupation as plastic surgeon.

34. On November 16, 2018, the Division issued to petitioners a statement of proposed audit changes, assessment number L-049133760, for the year 2015 (2015 statement), stating that “[t]he interest income on state and local bonds and obligations shown on your return does not agree with the amount(s) reported by the payer(s).” The 2015 statement explained:

“Interest income on obligations from any state other than New York State or any political subdivision of another state, though exempt from federal income tax, is taxable to New York State under NYS Tax Law sections 612(b)(1) and 1303.

You must report such income on line 20 of your 2015 personal income tax return.

All or part of the income that was credited to your account or which you received from the sources shown in the Fund details section of this notice was derived from non-New York State and local obligations. Because you did not make the proper line modification on your New York State return, we have adjusted your New York taxable income for the portion of the non-New York interest income included in your distribution(s) from these sources.”

The 2015 statement listed taxable amounts from several fund distributions of non-New York interest income made to petitioners totaling \$294,060.00, and indicated that petitioners reported \$0.00 of this amount on their 2015 return, resulting in a net adjustment of \$294,060.00. The 2015 statement noted that the Division’s computation of taxable income did not include interest from New York State or municipal sources.

The 2015 statement recalculated petitioners’ New York adjusted gross income to \$1,476,612.00, determined taxable income of \$1,460,762.00 and tax of \$100,062.00, and asserted tax due of \$20,143.00 plus interest.

35. On January 3, 2019, the Division issued to petitioners a notice of deficiency, assessment number L-049133760, asserting tax due of \$20,143.00 plus interest for tax year 2015.

36. On March 19, 2019, petitioners filed an amended resident income tax return, form IT-201-X, for 2015 (first 2015 amended return). On the first 2015 amended return, petitioners amended line 20, New York additions for interest income on non-New York state and local bonds and obligations, to \$294,060.00, and line 23, “other” New York additions, to \$0.00. Petitioners amended line 31, “other” New York subtractions to \$206,594.00. Petitioners reported New York adjusted gross income of \$1,179,913.00, claimed an itemized deduction of \$9,781.00, reported taxable income of \$1,170,132.00, and tax of \$90,488.00. Petitioners reported total payments of \$114,158.00, consisting of tax withheld of \$94,015.00 and amount paid with original return of \$20,143.00, and requested a refund of \$21,943.00. Petitioners reported Robert Ciardullo’s occupation as Doctor on the first 2015 amended return.

Petitioners attached to the first 2015 amended return a statement entitled “Form 225 as an

Attachment to Form 201X” wherein they indicated amortized bond premium of \$190,409.00 and accrued bond interest paid of \$16,185.00.

Also attached to the first 2015 amended return was correspondence from petitioners’ representative stating that the petitioners are protesting and appealing the 2015 statement and requesting that no refund be sent at this time.

37. Petitioners filed a second amended resident income tax return, form IT-201-X, for 2015 (second 2015 amended return), dated May 22, 2019. On the second 2015 amended return, petitioners amended the New York State itemized deduction schedule, reporting on line 11 of the schedule addition adjustments of \$190,410.00 and reporting on line 13 itemized deduction adjustment of \$219,616.00. The final itemized deduction amount reported of \$9,781.00 remained the same as the first 2015 amended return, and the amounts reported for taxable income, New York State tax, payments made and amount of refund claimed were the same as reported on the first 2015 amended return. Petitioners reported Robert Ciardullo’s occupation as surgeon on the second 2015 amended return.

Petitioners included with the second 2015 amended return a letter from their representative stating that they are protesting and appealing the 2015 statement and that they “contest the disallowance of amortized premium on IT 201D since it’s part of cost basis and is not interest income.”

38. On October 30, 2019, the Division issued to petitioners a notice of disallowance for 2015, sustaining assessment number L-049133760 which had been paid in full, and denying the refund claim of \$21,943.00. The notice of disallowance for 2015 states, “Bond premium amortization is not allowed as a direct offset to taxable municipal bond interest earned. Rather, it is allowable as an itemized deduction addition to be reported on Line 11 of the Form IT-201-D: Resident Itemized Deduction Schedule.”

39. Petitioners submitted into the record portions of 2015 Tax and Year-End Statements from Pershing LLC. The 2015 year-end statement for Robert Ciardullo shows federally tax-exempt interest income of \$140,703.16, specified private activity bond interest of \$12,575.00, bond premium on tax-exempt bonds for covered transactions of \$1,327.30, ordinary dividends of \$3.28, capital gain distributions of \$46.72, exempt interest dividends of \$69,030.06, and specified private activity bond interest dividends of \$12,192.21. The first page of the statement also shows a summary of form 1099-B with gross proceeds of \$2,915,000.00 and a cost basis of \$0.00, and refers to the 1099-B section of the statement for details. However, pages 2 through 11 of the 2015 year-end statement were not submitted by petitioners and the documents submitted do not contain the 1099-B section detail.

The 2015 year-end statement for Kira Ciardullo shows federally tax-exempt interest income of \$99,022.56, specified private activity bond interest of \$1,375.00, bond premium on tax-exempt bonds for covered transactions of \$839.08, ordinary dividends of \$1.36, capital gain distributions of \$18.88, exempt interest dividends of \$25,568.45, and specified private activity bond interest dividends of \$4,999.74. The first page of the statement also shows a summary of form 1099-B with gross proceeds of \$1,045,000.00 and a cost basis of \$0.00, and refers to the 1099-B section of the statement for details. However, pages 2 through 8 of the 2015 year-end statement were not submitted by petitioners and the documents submitted do not contain the 1099-B section detail.

2016

40. Petitioners filed a New York resident income tax return for 2016, dated May 11, 2017 (2016 initial return). On the 2016 initial return, petitioners reported federal adjusted gross income of \$819,360.00 consisting of wages, salaries and tips of \$606,633.00,¹³ taxable interest

¹³ Attached to petitioners' initial 2016 return are forms W-2, wage and tax statements for Robert Ciardullo

income of \$9,495.00, ordinary dividends of \$2,473.00, taxable refunds, credits or offsets of state and local income taxes of \$14,096.00, business income of \$1,786.00,¹⁴ capital gain of \$336.00,¹⁵ taxable amount of pensions and annuities of \$4,975.00, rental real estate, royalties, partnerships and S corporation income of \$179,692.00, and federal adjustment of \$126.00. On line 20 of the 2016 initial return, petitioners reported a New York addition for interest income on non-New York state and local bonds and obligations of \$132,675.00. For New York subtractions, on line 25, petitioners subtracted \$14,096.00 for taxable refunds, credits, or offsets of state and local income taxes; on line 29, petitioners subtracted \$4,975.00 for pension and annuity income exclusion; and on line 31, petitioners reported \$67,093.00 for “other.”

Petitioners reported New York adjusted gross income of \$865,871.00, claimed an itemized deduction of \$29,736.00, and reported taxable income of \$836,135.00, New York State tax of \$57,275.00, tax withheld of \$70,145.00, estimated payments of \$14,096.00, and requested that an overpayment of \$26,966.00 be applied to the following year’s estimated tax. The 2016 initial return lists Robert Ciardullo’s occupation as plastic surgeon.

41. On May 2, 2017, the Division issued to petitioners an account adjustment notice for 2016. The account adjustment notice states that petitioners’ New York itemized deductions were either added or computed incorrectly. The Division adjusted the total itemized deductions to \$29,650.00, recalculated petitioners’ taxable income to \$836,221.00, computed tax of \$57,281.14, and adjusted the claimed overpayment to \$26,959.86.

showing wages of \$603,896.51 from Robert C. Ciardulo MD PC, and for Kira Ciardullo from Westchester Health Associates, PLLC, showing wages of \$2,736.00.

¹⁴ A 2016 schedule C, profit or loss from business, reports the business income for Kira Geraci-Ciardullo MD, as medical doctor.

¹⁵ Petitioners’ 2016 schedule D, capital gains and losses, shows a short-term loss of \$3,261.00 and a long-term capital gain of \$3,597.00 for assets held for over one year. The transaction detail for the short-term loss showing dates of acquisition and sale is not included in the record.

42. Petitioners filed an amended resident income tax return, form IT-201-X, for 2016 (first 2016 amended return), dated May 22, 2019. On the first 2016 amended return, petitioners amended line 20, New York additions for interest income on non-New York state and local bonds and obligations, to \$0.00, and line 23, “other” New York additions, to \$132,675.00. Petitioners amended line 31, “other” New York subtractions to \$33,546.00. Petitioners reported New York adjusted gross income of \$899,418.00, claimed an itemized deduction of \$63,196.00, reported taxable income of \$836,222.00, and tax of \$64,065.00. Petitioners reported total payments of \$84,241.00, consisting of tax withheld of \$70,145.00 and estimated payments of \$14,096.00, and reported an overpayment of \$20,176.00.

Petitioners attached to the first 2016 amended return a statement that “Taxpayers compute Line 31 of IT 201X for Year 2016 as follows: $\frac{1}{2}$ of 67091 = 33546 from Line 11 IT-201D.” Petitioners also attached to the first 2016 amended return correspondence from their representative stating that the petitioners are protesting and appealing the disallowance of half the premium on IT 201D “since it’s part of cost basis and is not interest income. If you agree that the amount paid is correct, please refund the overpayment. If you disagree, please issue the Taxpayer an assessment of additional tax due which the Taxpayer will formally protest with the Division of Tax Appeals (DTA).”

43. On November 6, 2019, the Division issued to petitioners a statement of proposed audit changes, assessment number L-050909656, for the year 2016 (2016 statement), stating that “[t]he interest income on state and local bonds and obligations shown on your return does not agree with the amount(s) reported by the payer(s).” The 2016 statement contained the same explanation as the 2015 statement (see finding of fact 34) and stated the petitioners must report the interest income from non-New York sources on line 20 of the 2016 return.

The 2016 statement listed taxable amounts from several fund distributions of non-New

York interest income made to petitioners totaling \$133,489.00, and indicated that petitioners reported \$0.00 of this amount on their 2016 return, resulting in a net adjustment of \$133,489.00. The 2016 statement noted that the Division's computation of taxable income did not include interest from New York State or municipal sources.

The 2016 statement recalculated petitioners' New York adjusted gross income to \$1,032,907.00, determined taxable income of \$1,016,957.00 and tax of \$69,662.00, and asserted tax due of \$12,381.00 plus interest, and penalty of \$1,962.81.

Regarding the penalty, the 2016 statement explained:

“We have added a negligence penalty of 5% of the amount of additional tax due (section 685(b)(2) of the New York State Tax Law).

In addition to the 5% negligence penalty, an amount equal to 50% of any interest due on the deficiency or portion of a deficiency attributable to negligence has been imposed (section 685(b)(2) of the New York State Tax Law).

We computed the penalties for the following reason:

You have previously made the same error in computing New York tax and you were notified of the correct reporting requirements.”

44. On November 15, 2019, petitioners filed a second amended resident income tax return, form IT-201-X, for 2016 (second 2016 amended return). On the second 2016 amended return, petitioners amended line 20, New York additions for interest income on non-New York state and local bonds and obligations, to \$133,489.00, and line 23, “other” New York additions, to \$0.00. Petitioners reported New York adjusted gross income of \$900,232.00, claimed an itemized deduction of \$63,196.00, reported taxable income of \$837,036.00, and tax of \$57,337.00. Petitioners reported total payments of \$84,241.00, consisting of tax withheld of \$70,145.00 and estimated payments of \$14,096.00, reported an overpayment as shown on the original return of \$26,966.00, and reported an amount of tax owed of \$62.00.

45. On April 6, 2020, the Division issued to petitioners a notice of deficiency, assessment number L-050909656, and asserting tax due of \$12,381.00 plus interest, and penalty of \$2,200.22 for 2016.

46. Petitioners submitted into the record 2016 Tax and Year-End Statements from Pershing LLC. The 2016 year-end statement for Robert Ciardullo shows interest income of \$26.60, federally tax-exempt interest income of \$53,145.93, bond premium on tax-exempt bond covered transactions of \$17,253.39, ordinary dividends of \$23.82, capital gain distributions of \$360.99, exempt interest dividends of \$40,271.35, specified private activity bond interest dividends of \$6,139.24, and gross proceeds from broker and barter exchange transactions of \$2,009,979.68, with a cost basis for covered transactions of \$1,588,329.99. The proceeds from broker and barter exchange transactions consisted of three short-term transactions with a total loss of \$1,054.73 and several long-term transactions with a realized gain of \$5,659.42 for covered transactions and a realized gain of \$596.94 for non-covered transactions.

The 2016 year-end statement for Kira Ciardullo shows interest income of \$41.18, federally tax-exempt interest income of \$81,966.27, bond premium on tax-exempt bond covered transactions of \$12,164.94, ordinary dividends of \$29.19, capital gain distributions of \$41.38, exempt interest dividends of \$9,818.25, specified private activity bond interest dividends of \$1,622.30, and gross proceeds from broker and barter exchange transactions of \$2,627,338.55, with a cost basis for covered transactions of \$1,336,841.17. The 2016 form 1099-B, proceeds from broker and barter exchange transactions, shows a total realized loss of \$1,917.03 from three short-term transactions, a realized loss for long-term covered transactions of \$3,677.68, and a realized gain from long-term non-covered transactions of \$2.89.

CONCLUSIONS OF LAW

A. As New York state residents, petitioners' New York taxable income is their New York adjusted gross income (AGI) less New York deductions and New York exemptions (*see* Tax Law § 611 [a]). Petitioners' New York AGI equals their federal AGI with specific modifications, both increasing and decreasing federal AGI (*see* Tax Law § 612 [a]).

Included among the modifications increasing federal AGI for purposes of computing New York AGI is interest income on bonds issued by states other than New York, including political subdivisions of such states, to the extent not properly included in federal AGI (Tax Law § 612 [b] [1]).¹⁶ There is no dispute in this matter that interest income on petitioners' federally exempt municipal bonds was properly subject to New York income tax under this statutory add-back modification. The issue is whether "interest income" under Tax Law § 612 (b) (1) constitutes either the gross annual interest payments, or the gross annual interest payments less amortized bond premiums allocable to the year at issue. The issue raised here is identical to that in *Matter of Solomon* (Tax Appeals Tribunal, June 2, 2011), in which the Tax Appeals Tribunal (Tribunal) rejected the taxpayer's argument that interest income equals gross interest paid less amortized bond premiums allocable to the tax year and determined that interest income for purposes of New York tax law is the gross annual interest paid on the bonds.

Petitioners argue here, as did the taxpayer in *Matter of Solomon*, that pursuant to Tax Law § 607 (a), principles of federal conformity require that interest income under Tax Law § 612 (b) (1) be calculated as payments less bond premiums. Contrary to petitioners' argument, federal conformity does not extend to circumstances "[w]here a different meaning is clearly required" and is "subject to the exceptions or modifications prescribed by Article 22 or by statute" (*see* Tax

¹⁶ Tax Law § 612 (b) (1) provides the following to be added back into a taxpayer's federal adjusted gross income: "Interest income on obligations of any state other than this state, or of a political subdivision of any such other state unless created by compact or agreement to which this state is a party, to the extent not properly includible

Law § 607[a]; *see also Matter of Pospischil*, Tax Appeals Tribunal, June 6, 1996). Initially, it must be noted that this matter deals with income that is federally tax-exempt. Moreover, the Tax Appeals Tribunal has addressed the instant issue in *Matter of Solomon*, where it refuted the same claim that federal conformity required that New York treat the premiums paid on federally-exempt municipal bonds in the same manner as the Internal Revenue Code (IRC).

In *Matter of Solomon*, while noting that the Tax Law does not define interest income and that Tax Law § 607 (a) generally provides for conformity with the IRC, the Tribunal rejected the taxpayer's assertion that Tax Law § 607 (a) requires that interest income under Tax Law § 612 (b) (1) be calculated as payments less bond premium, stating, in part:

“In support of its position, petitioner references IRC § 171 and the regulations promulgated thereunder. These regulations provide that, with respect to a taxable bond, the bondholder must offset the periodic interest payments with the bond premium allocable to that period (*see* IRC § 171 [e]; Treas Reg § 1.171-2). Put alternatively, a taxpayer reports annual interest payment as the net of qualified stated interest less the relevant amortized bond premium. Petitioner also cites the historical treatment of amortized bond premiums, specifically the Technical and Miscellaneous Revenue Act of 1988 (Pub L 100- 647), as the reason for the dissonance between the IRC and Tax Law schemes. Petitioner argues that this is similar to *Matter of Friedsam* and that State legislative response was required to counter the federal change and retain the gross interest income definition.

We note that the federal conformity principle does not affect this matter because the Code does address the subject matter (Tax Law § 607 [a]). This is not a case where the Tax Law specifically references terms from the Code (*see e.g. Matter of Brookfield Power Corp.*, Tax Appeals Tribunal, November 10, 2010). Rather, Tax Law § 612(b)(1) calls for the treatment of interest income that is not included within the Federal adjusted gross income and must be added back at the state level.

We find that the New York scheme for addressing this income, generated from bonds issued by states other than New York, differs from the Code because the latter exempts such income from taxation while the former imposes tax, clearly requiring a different result (*c.f. Matter of Webster v. Tully*, 56 NY2d 532 [1982]). Accordingly, we hold that it is inappropriate to look to Federal law for guidance on federally tax-exempt municipal bonds because the Code is silent on such income.

We are not persuaded by petitioner's attempts to define interest income as the net of gross interest income less allocable bond premium. The Division's

understanding of interest income in Tax Law § 612(b)(1) as gross interest income is not only reasonable, but the same definition used in the Code. Form 1099-INT reports taxable and exempt interest income as gross interest income paid without an adjustment for the bond premium. IRS Publication 550 defines the offset as a separate adjustment to interest income. Treas Reg §§ 1.1016-5(b), 1.171-2(a) and Treasury Decision 8746 each identify the term interest income as separate and apart from the offset of the amortized bond premium provided by the Code. We find that this is not a situation where state legislative action was required to preserve the existing definition of interest income because there was no change (*c.f. Matter of Friedsam, supra*).

Contrary to petitioner's assertions, the 1988 modifications to the Code did not result in any change to the meaning of interest income, but in how bond premiums were reported. Treas Reg § 1.171-2(a), *Offsetting qualified stated interest with premium*, does not provide a definition of interest income, but provides guidance on how taxpayers account for the investment cost associated with taxable bond interest income. This regulation forces taxpayers to offset their investment costs by calculating an above-the-line 'amortized bond premium adjustment' (*see* IRS Publication 550, p. 36). While the definition of interest income remains the same as in the Code, the Tax Law imposes a different statutory scheme for addressing bond premiums, which is a below-the-line deduction (*see* Tax Law § 615[d][3]). In essence, petitioner objects to the New York statutory scheme that treats amortized bond premiums as below-the-line deductions. These objections are more appropriately directed to the Legislature. As such, we reject the argument that the Code provides a definition for interest income that includes amortized bond premium" (*id.*).

Petitioners raise the same argument here as the taxpayer in *Matter of Solomon*, objecting to the New York statutory scheme that treats amortized bond premiums as below-the-line deductions. The Tribunal's holding in *Matter of Solomon* is controlling, and petitioners' attempt to distinguish it is unavailing. Pursuant to *Matter of Solomon*, federally tax-exempt interest income for purposes of the Tax Law § 612 (b) (1) add-back means gross interest payments and not interest payments net of amortized bond premiums. Petitioners' argument that they are unable to claim the amortized bond premiums as an itemized deduction pursuant to Tax Law § 615 (d) (3), contending that such deductions are phased out for individuals in higher tax brackets, does not warrant a different result.

B. Petitioners further contend that Robert Ciardullo was engaged in a trade or business as a bond trader and as such they are entitled to subtract from their federal AGI ordinary and

necessary expenses paid for amortizable bond premiums pursuant to Tax Law § 612 (c) (10).

Tax Law § 612 (c) (10) provides for modifications reducing federal AGI in calculating New York AGI, stating that there shall be subtracted from federal AGI:

“Ordinary and necessary expenses paid or incurred during the taxable year for (i) the production or collection of income which is subject to tax under this article but exempt from federal income tax, or (ii) the management, conservation or maintenance of property held for the production of such income, and the amortizable bond premium for the taxable year on any bond the interest on which is subject to tax under this article but exempt from federal income tax, to the extent that such expenses and premiums are not deductible in determining federal adjusted gross income and are attributable to a trade or business carried on by the taxpayer.”

Petitioners have not met their burden of proof to show that bond premiums are attributable to a trade or business carried on by Dr. Ciardullo. Indeed, Dr. Ciardullo admits in his affidavit that, “I am not a bond broker/dealer, I am not a professional. I do not have a license and I do not buy bonds for other people – only for myself and my own account.” Rather, petitioner argues that, “I consider myself an ‘Investor/Trader’ or ‘Trader’” based on his control over his own bond transaction, his time spent researching transactions, and his volume and value of transactions. However, as discussed below, the attributes described by petitioner are not the determinative factors to consider for purposes of determining whether an individual is carrying on a trade or business.

A factual analysis in each case is required to determine if a particular taxpayer’s investment activities rise to the level of carrying on a trade or business (*see Higgins v Internal Revenue Serv.*, 312 US 212 [1941]; *Estate of Yaeger v Commissioner* (889 F2d 29, 33 [2d Cir 1989])). In determining whether an individual is engaged in a trade or business, the courts have distinguished between traders, who are considered to be engaged in a trade or business, and investors, who are not (*see e.g. Moller v United States*, 721 F2d 810, 811 [Fed Cir 1983]). A trader who earns a living buying and selling securities on an exchange may be carrying on a

trade or business, as opposed to an individual who is merely managing his own investments:

“A trader on an exchange, who makes a living in buying and selling securities or commodities, may be said to carry on a ‘business’; a person who frequents brokers’ offices, and continually dabbles in real estate is conceivably quite different. Most men who have capital change their investments, and may speculate all the time; we should hardly call this a business, though the line is undoubtedly hard to draw” (*Bedell v Commr. of Internal Revenue*, 30 F2d 622, 624 [2d Cir 1929]).

Similarly:

“Management of securities investments, whatever the extent and scope of such activity, is seen as the work of a mere investor, ‘not the trade or business of a trader.’ . . . This result is the same notwithstanding the amount of time the individual devotes to the activity. Even ‘full-time market activity in managing and preserving one’s own estate is not embraced within the phrase ‘carrying on a business,’ and * * * salaries and other expenses incident to the operation are not deductible as having been paid or incurred in a trade or business.’” (*Mayer v C.I.R.*, 67 TCM (CCH) 2949 [TC 1994] [citations omitted]).

In *Mayer*, the Court noted that sporadic trading will not constitute a trade or business.

Further, for a taxpayer’s activities to constitute the trade or business of trading, he must show that he seeks to catch the swings in the daily market movements, and to profit from these short-term changes. “In connection with this, courts look at whether the taxpayer’s securities income is principally derived from the frequent sale of securities rather than from dividends, interest, or long-term appreciation” (*Mayer v C.I.R.*).

Likewise, in *Estate of Yaeger v Commr.*, the Court explained the distinction between traders and investors as follows:

“Investors are engaged in the production of income. Traders are those ‘whose profits are derived from the direct management of purchasing and selling.’ Investors derive profit from the interest, dividends, and capital appreciation of securities. They are ‘primarily interested in the long-term growth potential of their stocks.’ Traders, however, buy and sell securities ‘with reasonable frequency in an endeavor to catch the swings in the daily market movements and profit thereby on a short term basis’” (*Estate of Yaeger v Commr.*, citations omitted).

The Court noted that the two fundamental criteria that distinguish traders from investors is the length of the holding period and the source of the profit, and determined that the taxpayer was an investor, despite having initiated over 2000 trades in two years,

and despite the finding that he pursued his security activities vigorously and extensively (*id.*). The Court explained that “[n]o matter how large the estate or how continuous or extended the work required may be, the management of securities investments is not the trade or business of a trader (*id.*, citing *Higgins v Internal Revenue Serv.*, 312 US at 218).

Petitioners here argue that during the five years at issue, Dr. Ciardullo made over 500 bond purchases and sales transactions, a number far less than the taxpayer’s transactions in *Estate of Yaeger v Commr.* Moreover, contrary to petitioners’ argument, the number of trades or the time spent managing their investments is not relevant to the determination (*id.*). Rather, the courts look at the length of the holding period and the source of the profit:

“More importantly, most of his sales were of securities held for over a year. He did not sell any security held for less than three months. He realized a profit on the securities through both dividends and interest. Most of his profit, however, came from holding under valued stock until its market improved. This emphasis on capital growth and profit from resale indicates an investment motivated activity. See *Miller v. Commissioner*, 70 T.C. 448, 457 (1978). In addition, since the income came from long-term appreciation, Yaeger would receive the benefit of favorable capital gains treatment. To disregard the nature of the income and length of his holdings simply because Yaeger was a vigorous investor would defeat the purpose of section 163(d)” (*Estate of Yaeger v C.I.R.*, 889 F2d 29, 34 [2d Cir 1989]).

The record here shows that like the taxpayer in *Estate of Yaeger*, petitioners held most of the securities long-term and most of the profit was derived from interest income, rather than from frequent short-term buying and selling. As such, petitioners have failed to meet their burden of proving that they were carrying on a trade or business with their investment activities.

Petitioners’ attempt to distinguish their bond investment from other securities in regard to short term profit taking, contending that due to market rates they could not make a short-term profit, is on no avail. Indeed, petitioners’ failure to show that Dr. Ciardullo sought to catch the swings in the daily market movements belies their argument that he is in the trade or business of

a trader. The courts have repeatedly found the distinction between income derived from short-term profits, as opposed to income from dividends, interest, or long-term appreciation to be determinative. The record shows that Dr. Ciardullo is not in the trade or business of a trader. Rather, he is a doctor managing his own personal investments in his and his wife's accounts.

C. Petitioners further contend the taxation of gross interest income paid on bonds issued by states other than New York violates the New York and United States Constitutions. Petitioners' argument challenges the constitutionality of the applicable provisions of the Tax Law on its face, and not on an "as applied" basis. The Division of Tax Appeals lacks jurisdiction over such constitutional challenges, and statutes are presumed to be constitutional on their face (*see Matter of Eisenstein*, Tax Appeals Tribunal, March 27, 2003; *see also Matter of Geneva Pennysaver*, Tax Appeals Tribunal, September 11, 1989; *Matter of Fourth Day Enters.*, Tax Appeals Tribunal, October 27, 1988). Petitioners have not shown the New York's taxing scheme violated the New York or United States Constitutions on an "as applied" basis, in that they have not shown that the Division applied the Tax Law to petitioners in a manner different than any other similarly situated taxpayer (*see Matter of HDV Manhattan, LLC*, Tax Appeals Tribunal, February 12, 2016; *Matter of Finch, Pruyn & Co., Inc.*, Tax Appeals Tribunal, April 22, 2004). Accordingly, the Division of Tax Appeals does not have jurisdiction to consider this particular argument advanced by petitioners.

D. The petitions of Robert and Kira Ciardullo are denied, and the notices of deficiency, dated April 4, 2016, January 3, 2019, and April 6, 2020, and notices of disallowance dated August 31, 2016, May 30, 2019, and October 30, 2019, are sustained.

DATED: Albany, New York
November 10, 2021

/s/ Barbara J. Russo
ADMINISTRATIVE LAW JUDGE