

TAX APPEAL BOARD OF THE STATE OF DELAWARE

Estate of EVELYN F. STOLTZ
Petitioner,

v.

DIRECTOR OF REVENUE,
Respondent.

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) DOCKET NO. 874
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Before: Joseph S. Yucht, Esquire, Chairman; John H. Cordrey, Esquire, Vice Chairman;
Harry B. Roberts, David Eppes and Regina Dudziec, Members.
Johannes R. Kraemer, Esquire (argued) and John S. McDaniel, Esquire, of Morris, Nichols,
Arsht & Tunnell for Petitioners.
Joseph Patrick Hurley, Jr., Esquire, Deputy Attorney General for Respondent.

DECISION AND ORDER

John H. Cordrey, Esquire, Vice Chairman. The parties have stipulated to the facts of the case which are contained in the stipulation attached hereto as "Exhibit A" and made a part hereof by reference. A brief summary of the facts show that the Petitioner is the Estate of Evelyn F. Stoltz who died on March 7, 1985. Mrs. Stoltz, during the tax year 1981 operated an accrual basis sole proprietorship which conducted a real estate business, Stoltz Realty Company ("Realty"). During tax year 1981, Arbern Wilmington, Inc. ("Arbern") made a purchase through Realty entitling Realty to a commission of \$480,000. Payment of the commission, pursuant to a requirement of the financing institution of Arbern and the agreement of the parties, was delayed until such time as the mortgage on the building was paid. No portion of the commission was paid until 1984 at which time Realty included the portion it received in its gross income.

Petitioner argues that, as the Delaware personal income tax statute is a "piggyback"

tax, the adjusted gross income (hereinafter "AGI") as reported in good faith on the federal return, which is not subsequently modified by the federal authorities within the Statute of Limitations, is the beginning point for determining the State income tax. In support of this position Petitioner cites 30 Del.C. Section 1105 which provides:

The entire taxable income of a resident of this State shall be his adjusted gross income as defined in the laws of the United States with the modifications and less the deductions and personal exemptions provided in this chapter.

The statute does require the use of the federal AGI but "...as defined in the laws of the United States..." Implicit in the statute is the requirement that the determination of the federal AGI be made correctly in accordance with federal law. If the reported AGI on the federal form is not calculated correctly (whether through miscalculation, fraud, misinterpretation of a statute, etc.) it is not the AGI defined in the laws of the United States.

As a taxpayer is required to start his determination of his Delaware tax by a correctly determined federal AGI, the taxpayer may not submit a figure for his AGI, even though it is admittedly the same figure provided on his federal return, and require that the State be bound by that figure. Petitioner's argument that the federal government failed to modify the AGI on Petitioner's federal form within the appropriate statute of limitations is without foundation in the factual stipulation of the parties. Even assuming that the assertion was before the Board and true, the fact that the Federal government failed to modify the AGI of Petitioner does not mean that it is calculated in accordance with the appropriate federal statutes. The federal government might not have audited the return, let alone considered the specific issues raised by the State.

Petitioner argues in the reply brief that while the Respondent is not bound by a fraudulent, negligent or mistaken reported AGI, the Respondent should be bound by a good faith reported AGI if not modified by the federal government. The difference between the

positions is neither existent nor relevant to the inquiry. The *mens rea* of the taxpayer is not the question, rather the question is whether the taxpayer's AGI is correctly calculated in accordance with the laws of the United States.

Petitioner also contends Respondent is prohibited from reviewing the AGI reported by the taxpayer and not adjusted by the federal authorities within the applicable statute of limitations. Contrary to Petitioner's position, Respondent is permitted through 30 Del.C. Section 1181 to audit and make adjustments to returns.

As the Respondent is permitted to perform audits upon returns and is not bound by the AGI figures reported on the Taxpayer's return, the Board must turn to the central issue of this case, whether the accrual basis taxpayer's right to receive a commission is fixed and unconditional such that it is reportable in 1981.

Petitioner is an accrual basis taxpayer and therefore the income shall be included in the Petitioner's income in the year during which all events have occurred that fix the right to receive the income and the amount of the income can be determined with reasonable accuracy. By its very definition this is the case even though actual payment is deferred.

In the case at bar, Petitioner had performed such acts as were necessary to earn the sales commission, yet it was not paid in 1981. It was not paid because the Bank financing the conversion project required the payment of its outstanding mortgage prior to the payment of the sales commission and all parties agreed to that condition. Petitioner suggests that the right to the income is either "contingent or subject to a condition precedent" or "collectibility of the income is doubtful" either of which entitles Petitioner not to accrue the income in 1981.

Numerous Courts have held that accrual of income is not required when the collection of the income is shown to be doubtful, but almost all cases so holding have or require a

showing of insolvency, receivership, or similar clear indication of the inability to complete the payments required. American Fork & Hoe Co. v. Commissioner, 33 B.T.A. 1139 (1936), Jones Lumber Co. v. Commissioner of Internal Revenue, 6th Cir., 404 F.2d 764 (1968). Contrary to the assertions of Petitioner, the Board cannot support a finding, based upon the record present in this case, that the receipt of the income was sufficiently doubtful to permit Petitioner to not accrue the income.

As to the claim that the income is contingent, the Board finds there to be no contingency which would prohibit the accrual of the income. The income was earned by the Petitioner at the time that the services were completed and the amount of compensation can be determined, that occurred in 1981. That the payment of the income was "contingent" upon the prior payment of a mortgage upon the premises is not such a contingency as to prevent accrual of the income. Petitioner had performed all acts necessary from her to earn the income, payment was merely delayed until some point in the future when the mortgage upon the property was retired. That was merely a delay in time of payment, not a contingency.

Petitioner having chosen the accrual method of tax accounting must be bound by the bad as well as the good consequences of the election. If the income had properly been reported in 1981 and subsequently it became obvious all or some portion was not to be paid, a claim for a bad debt deduction could be made.

For the foregoing reasons the Director's determination is Affirmed.

IT IS SO ORDERED, this 11th day of May, 1990.

John H. Lindsey
Regina C. Hudgins
David B. Whitcomb

Joseph P. Jones

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TAX APPEAL BOARD

ESTATE OF EVELYN F. STOLTZ,)
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 Petitioner,)
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 v.) Docket No. 874
)
 DIRECTOR OF REVENUE,)
)
 Respondent.)

STIPULATION OF FACTS

It is stipulated by and between the Estate of Evelyn F. Stoltz and the Director of Revenue that the following facts shall be accepted as true for purposes of this proceeding:

1. The Petitioner is the Estate of Evelyn P. Stoltz, whose address was 616 Devon Apartments, 1401 Pennsylvania Avenue, Wilmington, Delaware 19806. Evelyn F. Stoltz died on March 7, 1985. Her executor is Morris L. Stoltz, II. Morris L. Stoltz, II and Jack P. Stoltz are the sons of Evelyn F. Stoltz.

2. During the calendar year 1981, Evelyn F. Stoltz owned a sole proprietorship known as Stoltz Realty Company ("Realty"). Realty employed the accrual method of accounting. Morris L. Stoltz, II and Jack P. Stoltz are on the cash basis method of accounting.

3. During the calendar year 1981, Realty performed services for Arbern Wilmington, Inc. in connection with the purchase by Arbern Wilmington, Inc. of the apartment building located at 1401 Pennsylvania Avenue ("1401 Apartments") from 1401 Associates, L.P. for the sum of \$4,820,000.00. Arbern Wilmington agreed to pay Realty a sales commission of \$480,000 for such services. Said sales commission was subordinated to a first mortgage loan commitment in the amount of \$6,356,250.00 to Wilmington Trust Company. Paragraph 2 of the loan commitment letter from Wilmington Trust Company dated January 22, 1981 provided as follows:

"2. Subordination of Sales Commissions:
 Any sales commission payable by the purchaser, its successors, assigns or nominee, under the contract of sale between 1401 Associates, L.P., Seller, and Arbern Wilmington, Inc., Purchaser,

for acquisition of the Project, or otherwise related to your acquisition of the Project, shall be fully subordinated to the Mortgage and to the prior payment in full of all sums secured by the Mortgage."

4. The Wilmington Trust Company Mortgage was not fully paid until 1984 after Arbern Wilmington had completed its conversion of the units in the 1401 Apartments into condominiums, and the sale of most of those units.

5. In 1984 Arbern Wilmington paid Realty \$150,000 of the \$480,000 commission owed, and in 1985 Arbern Wilmington paid Realty \$175,000 of the \$480,000 commission owed. One large condominium unit in the 1401 Apartments has not yet been sold by Arbern Wilmington.

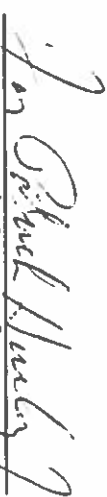
6. Arbern Wilmington employed the accrual method of accounting and accrued the \$480,000 in commission expense in 1981.

7. The amounts of the foregoing commissions were included in the gross income of Realty in the year in which paid. Realty did not accrue the \$480,000 sales commission in 1981.


8. On January 24, 1981 Realty executed a Note signed by Evelyn F. Stoltz as its sole proprietor, payable to Jack P. Stoltz and Morris J. Stoltz, in the total amount of \$480,000 for the services of Jack P. Stoltz and Morris L. Stoltz, II on behalf of Realty in connection with the aforesaid commission. The said Note, a copy of which is attached hereto as Exhibit "A" provides that the amount thereof is payable "if, as, when, and if Stoltz [Realty] receives the sales commission from Arbern Wilmington, Inc. on the sale of 1401 Apartments to Arbern Wilmington, Inc."

9. When Realty received the payment of \$150,000 from Arbern Wilmington in 1984, and the payment of \$175,000 from Arbern Wilmington in 1985, Realty paid those same amounts to Jack P. Stoltz and Morris L. Stoltz, II, which amounts Jack P. Stoltz and Morris L. Stoltz, II included in their gross incomes in those years.

IN WITNESS WHEREOF, we have hereunto set our hands and seals this 20th day of September, 1987.


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for Division of Revenue

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