

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition :
of :
HAL AND JULIE MITNICK : DECISION
for Redetermination of a Deficiency or for :
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Year 1984. :

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on June 28, 1990 with respect to the petition of Hal and Julie Mitnick, 60 East End Avenue, Apt. 7B, New York, New York 10028, for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the year 1984 (File No. 805672). Petitioners appeared by Kenneth Mersel, C.P.A. The Division of Taxation appeared by William F. Collins, Esq. (Lawrence A. Newman, Esq., of counsel).

Both petitioners and the Division of Taxation filed briefs on exception.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUE

Whether medical diagnostic equipment which was possessed by petitioners under lease agreements was "acquired by purchase" within the meaning of Tax Law § 606(a)(2).

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge and make additional findings of fact. The Administrative Law Judge's findings of fact and the additional findings of fact are set forth below.

Petitioners Hal and Julie Mitnick filed a joint New York State personal income tax return for 1984. On the return, petitioners claimed an investment tax credit of \$10,864.00.

Petitioners claimed the investment tax credit in question on the lease of medical diagnostic imaging equipment that is used to produce X-rays. Petitioner Julie Mitnick, M.D., a sole proprietor, is a specialist in radiology. In 1984 Dr. Mitnick leased plain film and IVP processing equipment from the General Electric Company and mammography diagnostic equipment from Philips Medical Systems, Inc. Both units were installed and in operation in 1984.

On March 11, 1988, the Division of Taxation issued to petitioners a Notice of Deficiency for 1984 which asserted personal income tax due of \$10,862.34 plus interest. The notice of deficiency resulted from the Division's disallowance of the investment tax credit claimed by petitioners on the medical diagnostic imaging equipment.¹ The investment tax credit was denied by the Division on the basis that the X-ray equipment was not used to produce goods by manufacturing or processing.

In addition to the facts found by the Administrative Law Judge we find the following.

In the audit report introduced by the Division it is stated "T/P claimed investment tax credit on 2 xray machines T/P had on lease in 1984. T/P could prove only one. Other one was as per invoice placed in service in 1985. Looked into law discussed with T/L. Xray machine is not considered to be used for processing as per NY State law and hence investment credit disallowed."

In item number 6 of their petition, petitioners stated:

"1) The tax commission disallowed a NYS investment credit on machinery which they said is not principally used in one of the areas stated in the Law as allowable.

"2) The machinery in question is processing equipment, used in radiology procedures.

"3) The NYS tax law specifically includes equipment used in processing as eligible for NYS investment tax credit."

In its answer the Division stated as follows:

¹The \$1.66 difference between the amount claimed as the investment tax credit and the amount disallowed appears to be the result of the rounding off of figures in the computation of tax due. The difference has no effect on this determination.

"1. DENIES each and every allegation set forth at item 6 of the perfected petition wherein the petitioner states his grounds upon which relief is claimed.

"2. AFFIRMATIVELY STATES that this deficiency consisted of the investment credit being disallowed, in that x-ray processing equipment does not qualify for the credit.

"3. AFFIRMATIVELY STATES that the petitioner has the burden of proving wherein the assessment is erroneous and/or improper."

At the hearing, the Division raised the issue of whether the equipment at issue was acquired in 1984, the year in which the credit was claimed. The Administrative Law Judge treated this as a request by the Division to amend its answer and allowed petitioners 30 days to submit evidence on the question of when the equipment was acquired.

After the hearing, petitioners submitted evidence with respect to the acquisition of the equipment including evidence of a lease agreement with respect to each piece of equipment. The Division commented on this submission, stating that it was inadequate to prove that the equipment was acquired in 1984, but never asserted that the equipment could not qualify for the investment tax credit because it was acquired by lease.

OPINION

The Administrative Law Judge granted the petition and cancelled the Notice of Deficiency of petitioners, determining that petitioners' medical diagnostic equipment was used in the production of goods by manufacturing and processing within the meaning and intent of Tax Law former § 606(a)(2), thus qualifying for an investment tax credit.

On exception, the Division of Taxation (hereinafter the "Division") does not except to the Administrative Law Judge's determination that petitioners' equipment was used in processing within the meaning of Tax Law former § 606(a)(2). Instead, the Division contends for the first time that the Division's denial of petitioners' claim for an investment tax credit should be sustained because the equipment was not acquired by purchase.

More particularly, in its exception, the Division requests the following as a conclusion of law:

"Although at the hearing, the Division of Taxation did not challenge the claimed investment tax credit on the grounds that the equipment at issue was not purchased within the meaning of the internal revenue code. The documents submitted post-hearing by the petitioners evidence a lease of the equipment, rather than acquisition by purchase. Consequently, the property does not qualify for the investment tax credit."

In response, petitioners assert that the terms of the lease agreements and the conduct of the parties during and subsequent to the lease term conferred "equitable ownership" of the equipment upon petitioners. Accordingly, petitioners contend that the transactions should be treated as purchases for Federal income tax purposes, thus entitling them to the investment tax credit.

We affirm the determination of the Administrative Law Judge.

Other than its general reference to the Internal Revenue Code, the Division has cited no support for its assertion that a lease is not an acquisition by purchase. Our own review of this issue indicates that section 606(a)(2) of the Tax Law states that the property must be "acquired by purchase as defined in section one hundred seventy-nine (d) of the internal revenue code." Purchase is defined in section 179(d)(2) of the Internal Revenue Code as "any acquisition of property" so long as the property is not acquired from certain related persons, from a decedent or in a transfer where the basis of the property is determined based on the transferor's basis in the property. We see nothing in this definition of purchase which excludes the acquisition of the property at issue.² Accordingly, we affirm the determination of the Administrative Law Judge.

We cannot account for the Division's handling of this case. Although the Division knew since the time of the audit that the instant equipment was leased (Division's Exhibit D, Audit Report), the Division never attempted to raise this as an issue until after the Administrative Law Judge's determination was issued. Now that the Division has attempted to raise this issue by filing an exception, it has offered absolutely no support for its position that a lease is not an

²The Division's assertion that a lessee can never qualify for the investment tax credit because the lessee has not acquired the property by purchase is contrary to the Division's regulations which allow a lessee to take the credit provided the other conditions of section 606(a)(2) are satisfied, e.g., that the property is depreciable pursuant to section 167 of the Internal Revenue Code (an issue that has not been raised here).

acquisition by purchase. This conduct evidences a total disregard for the taxpayer's right to have a just system for resolving controversies with the Division and our responsibility to provide such a system (Tax Law § 2000).

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Hal and Julie Mitnick is granted; and
4. The Notice of Deficiency dated March 11, 1988 is cancelled.

DATED: Troy, New York
January 25, 1991

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner

/s/Maria T. Jones
Maria T. Jones
Commissioner