STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
BOENING BROS., INC.	:	DECISION DTA No. 810740
for Redetermination of a Deficiency or for Refund of Corporation Franchise Tax under Article 9-A of the Tax Law for the Fiscal Years Ending March 31, 1983 and March 31, 1986.	:	

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on November 10, 1993 with respect to the petition of Boening Bros., Inc., 1098 Route 109, North Lindenhurst, New York 11757. Petitioner appeared by Spahr, Lacher & Sperber (Jack Mitnick, CPA). The Division of Taxation appeared by William F. Collins, Esq. (Vera R. Johnson, Esq., of counsel).

The Division of Taxation filed a brief on exception. Petitioner filed a brief in opposition. The Division of Taxation filed a reply brief which was received on June 10, 1994 and began the six-month period for the issuance of this decision. The Division of Taxation's request for oral argument was denied.

Commissioner Dugan delivered the decision of the Tax Appeals Tribunal. Commissioner Koenig concurs.

ISSUE

Whether the entire amount of bottle deposits shown on petitioner's books at the end of the fiscal year ending March 31, 1986 should be included as income for such year rather than only the increased amount reflected on petitioner's books, i.e., the difference between the container deposits payable at the end of the fiscal year ending March 31, 1985 and the container deposits payable at the end of the fiscal year ending March 31, 1986.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Petitioner, Boening Bros., Inc. ("Boening"), as a beverage distributor operating in the Metropolitan Commuter Transportation District during the years at issue, charged its customers for container deposits pursuant to the "New York State Returnable Container Act" (L 1982, ch 200), as codified atArticle 27, Title 10, "Litter and Solid Waste Control", of the Environmental Conservation Law ("ECL"). Pursuant to ECL 27-1005, included in petitioner's receipts from the sale of beverages were "refund values", commonly referred to as "bottle deposits." Pursuant to ECL 27-1007, when an empty beverage container of the type sold by Boening was returned to it, Boening paid the refund value (deposit) to the "dealer or operator of a redemption center."[1]

Petitioner accounted for its receipt of "bottle deposits" on its books as "unredeemed container deposits payable,"[2] which increased as follows:

Fiscal Year Ending	Unredeemed Container Deposits Payable	Increase from Prior Year
March 31, 1984	$1,053,652.00	--------
March 31, 1985	1,536,395.00	$482,743.00
March 31, 1986	1,650,832.00	114,437.00

Petitioner reported entire net income (loss) of ($211,259.00) on its corporation franchise tax returns for the fiscal year ending March 31, 1986. It paid CT-3 (corporation franchise) taxes

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[1]The parties in their stipulation dated March 2, 1993 used the term "redeemer" as the party to whom Boening paid the refund value. However, ECL 27-1003.8 defines the term "redeemer" to mean "every person who demands the refund value provided for herein in exchange for the empty beverage container, but shall not include a dealer as defined in subdivision four of this section." "Dealer" is defined as "every person, firm or corporation who engages in the sale of beverages in beverage containers to a consumer for off premises consumption in this state." It would appear that Boening as a "distributor," which is defined at ECL 27-1003.6 as "any person, firm or corporation which bottles, cans or otherwise fills or packages beverage containers, or which engages in the sale of such containers to a dealer," paid the "refund value" to the "dealer or operator of a redemption center," who earlier had paid the "refund value" to a "redeemer."

[2]This apparently was the terminology used by petitioner on its books to account for bottle deposits received upon the sale of beverage containers to dealers.

of $14,473.00 and CT-3M (Metropolitan Transportation Business Tax Surcharge) taxes of $2,460.00.

The Division of Taxation ("Division") audited petitioner's corporation franchise tax reports for the fiscal years ending March 31, 1983, March 31, 1986 and March 31, 1987.[3] On audit, the Division treated the "unredeemed container deposits payable" as income. A Statement of Franchise Tax Audit Changes dated January 30, 1989 showed the following computation of tax due for the two years at issue herein:

	Fiscal Year Ended March 31, 1983	Fiscal Year Ended March 31, 1986
Income reportable from container deposits	___[4]	$1,650,832.00
Truck & Auto		400,979.00
Travel & Entertainment		60,064.00
Salesman & Auto		83,560.00
Net operating loss carryback disallowed	$211,259.00	
Net adjustment	$211,259.00	$2,195,435.00
Taxable income previously stated	0.00	(211,259.00)
Corrected taxable income	$211,259.00	1,984,176.00
Tax due	21,125.90	198,417.60
Add: Metropolitan Trans. Business Tax Surcharge	3,591.40	33,730.99
Corrected tax due	$ 24,717.30	$ 232,148.59
Tax previously computed	0.00	16,933.00
Additional tax due	$ 24,717.30	$ 215,215.59
1085(B) penalty	---	$ 10,760.78

Because the net operating loss for the fiscal year ended March 31, 1986 was eliminated, the net operating loss carryback to the fiscal year ended

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[3] The results of the audit of March 31, 1987 are not at issue herein.

[4] The law requiring bottle deposits (L 1982, ch 200) became effective July 1, 1983 which would explain the lack of an entry for "income reportable from container deposits" for the fiscal year ended March 31, 1983. The record does not disclose if the fiscal years ended March 31, 1984 and March 31, 1985 were audited.

March 31, 1983 was eliminated.

Four notices of deficiency, all dated June 14, 1989, correspond, for the most part,[5] to the Statement of Franchise Tax Audit Changes. They asserted tax due of $21,125.90 plus interest for the year ended March 31, 1983, tax due of $3,591.40 plus penalty for the year ended March 31, 1983 (representing the Metropolitan Transportation Business Tax Surcharge), tax due of $183,944.60 plus penalty and interest for the year ended March 31, 1986, and tax due of $31,270.99 plus penalty and interest for the year ended March 31, 1986 (representing the Metropolitan Transportation Business Tax Surcharge), respectively.

A conciliation order dated February 14, 1992 resulted in the reduction of tax asserted as due for the fiscal year ending March 31, 1986 as follows:

(1) CT-3 tax asserted as due reduced from $183,944.60 plus penalty and interest to $130,743.20 plus penalty and interest.

(2) CT-3M tax asserted as due reduced from $31,270.99 plus penalty and interest to $22,226.75 plus penalty and interest. According to the parties' stipulation dated March 2, 1993, these reductions were based upon "reasons unrelated to the controversy at bar." The stipulation also noted that the notices of deficiency issued for the fiscal year ended March 31, 1987 were cancelled by the conciliation order also "[f]or reasons unrelated to the issues at bar." In sum, the parties noted that the conciliation order "reflects a total deficiency of $177,687.25 of which $152,969.95 [$130,743.20 plus $22,226.75] is attributable to the FYE March 31, 1986 and $24,717.30 is attributable to the FYE March 31, 1983."

The record does not disclose petitioner's actual treatment of the bottle deposits, i.e., whether they were physically segregated in any way from its general funds or were, instead, commingled with other receipts. It also does not explicitly disclose whether petitioner's "unredeemed container deposits payable" account, as noted above, represents a net amount after the deduction for container deposits which have been paid to dealers or operators who have returned empty containers to petitioner, as a distributor, for redemption of the "refund values." Furthermore, it is not known whether handling fees of 1.5 cents per container required under

[5]The Notice of Deficiency for the period ending March 31, 1983 asserting the Metropolitan Transportation Business Tax Surcharge of $3,591.40 also showed penalty of $2,911.87 while the Statement of Franchise Tax Audit Changes did not show penalty added to the surcharge. However, it is observed that no interest was asserted in the Notice of Deficiency for the earlier fiscal year. Perhaps the penalty of $2,911.87 was, in fact, interest calculated due.

ECL 27-1007(3) to be paid to a dealer or operator of a redemption center who returns empty containers to petitioner, as a distributor, have been netted out against this "unredeemed container deposits payable" account.

Relevant portions of the stipulation dated March 2, 1993 have been incorporated into these Findings of Fact.

OPINION

At hearing, the parties stipulated that:

> "[t]he controversies before the Division of Tax Appeals in the matter at bar are whether the Division correctly recomputed the Boening's entire net income for the FYE March 31, 1986 by including the container deposits payable as income; and if so, whether the entire amount reflected on Boening's books at the end of the FYE March 31, 1986 may be included as income for the fiscal year ending March 31, 1986 rather than the increased amount reflected on Boening's books, representing the difference between the container deposits payable at the end of the FYE March 31, 1985 and the container deposits payable at the end of the FYE March 31, 1986 ($114,437.00)" (Stipulation, ¶ 12).

The Administrative Law Judge, based on his review of Dana Distribs. v. Commissioner (56 TCM 569, affd 874 F2d 120 [New York State bottle bill]); Colonial Wholesale Beverage Corp. v. Commissioner (55 TCM 1736, affd 878 F2d 23 [Massachusetts bottle bill]); Wilson v. Commissioner (51 TCM 811 [Michigan bottle bill]); Fred Nesbitt Distrib. Co. v. United States (604 F Supp 552 [Iowa bottle bill]), found that "(1) bottle deposits are includable in income in the year of receipt and (2) no deduction is allowable for deposits which the taxpayer expects to refund" (Determination, conclusion of law "D"). The Administrative Law Judge found the decision in the Dana case persuasive:

> "[t]he law governing the taxability of amounts collected on the sale of items returnable to the seller is well-established. 'Deposits' on containers are includable in income if the containers are sold along with their contents (Okonite Co. v. Commissioner, 4 T.C. 618, 628 [1945], affd 155 F.2d 248 (3d Cir. 1946), cert. denied 329 U.S. 764 (1946). The later return of the container for a 'refund' of the 'deposit' is considered a resale" (Dana Distribs. v. Commissioner, supra).

In Dana, the Tax Court determined that the beverage distributor therein sold the containers along with their contents for three reasons:

> "[f]irst, the sales invoices contained no title retention clause. Second, petitioner did not place its name on the containers or exhibit any other effort to control disposition of the containers. Third, petitioner had no enforceable right to compel the retail stores, bars, restaurants, or individual consumers to return the containers. While there is an economic incentive to return the containers, under New York law the buyers are free to keep the containers, dispose of them or return them to other distributors besides petitioner" (Dana Distribs. v. Commissioner, supra).

The Administrative Law Judge rejected petitioner's assertion that Commissioner v. Indianapolis Power & Light Co. (493 US 203) effectively overruled Dana Distribs. v. Commissioner (supra), stating:

> "[t]he Division's argument that the matter at hand involves two transactions not one as in Commr. v. Indianapolis Power and Light Co. (supra) provides a ready way to distinguish the situation at hand. Unlike the situation in Oak Industries v. Commr. (52 TCM 1556), where the electronic decoder box was never sold to the subscriber, petitioner sold the beverage container along with the beverage. When the empty container was returned for its deposit, it was resold back to petitioner" (Determination, conclusion of law "F").

The Administrative Law Judge determined, however, that only the difference between the container deposits payable at the end of the fiscal year ending March 31, 1985 and the container deposits payable at the end of the fiscal year ending March 31, 1986 may be included in petitioner's entire net income for the fiscal year ending March 31, 1986. Specifically, he concluded that:

> "[i]ncluding the entire amount shown on Boening's books for container deposits payable at the end of the fiscal year ending March 31, 1986 of $1,650,832.00, instead of the difference of $114,437.00, would not properly reflect Boening's entire net income for its fiscal year ending March 31, 1986. As noted in Finding of Fact "2", it appears that Boening received the major part of its bottle deposits (which it never paid back to dealers or operators of redemption centers) during the first year of the implementation of the bottle bill or during its fiscal year ending March 31, 1984. By the time the Division audited Boening, the statute of limitations apparently barred an assessment for this earlier year. The Division may not now utilize Tax Law § 208(9)(d) as a way around the statute of limitations since including the entire amount of $1,650,832.00 would not properly reflect Boening's entire net income for the fiscal year ending March 31, 1986. In short, income from bottle deposits is properly included in the year of receipt (cf., Schlude v. Commr., 372 US 128, 83 S Ct 601, 9 L Ed 2d 633)" (Determination, conclusion of law "G").

On exception, the Division asserts that the Administrative Law Judge was wrong when

he determined that:

> "[t]he Administrative Law Judge erred in concluding that the statute of limitations bars the Division from taxing container deposits received during the closed years. Given the nature of the audit adjustment -- a change in the method of accounting for the receipts, the statute of limitations provisions are not violated. When a change of accounting methods would result in omitting income, that income is taxable in the year of the accounting change" (Division's brief on exception, pp. 3-4).

The Division relies on Tax Law § 208(9)(d) and 20 NYCRR 2-2.1, 20 NYCRR 2-2.2 and 20 NYCRR 3-2.8 for its position. Section 208(9)(d) provides that the Division "may, whenever necessary in order properly to reflect the entire net income of any taxpayer, determine the year or period in which any item of income or deduction shall be included, without regard to the method of accounting employed by the taxpayer." 20 NYCRR 2-2.1, 20 NYCRR 2-2.2 and 20 NYCRR 3-2.8 implement the statutory language.[6]

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[6]20 NYCRR 2-2.1 provides:

> "General. [Tax Law, § 208(9)] (a) The accounting method or basis on which entire net income is to be computed must be the same as the taxpayer's method of accounting for Federal income tax purposes. However, when the Commissioner of Taxation and Finance deems it necessary in order to properly reflect the entire net income of the taxpayer, it may determine the taxable year or period in which any item of income or deduction must be included, without regard to the method of accounting used by the taxpayer. (See section 3-2.7 of this Title -- Taxable year in which income or deduction is included in entire net income.)
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> (b) In the absence of an accounting method for Federal income tax purposes, entire net income must be computed in accordance with the method regularly employed in keeping the books of the taxpayer, provided such method properly reflects entire net income. If the books of a taxpayer do not properly reflect entire net income, or if no books are kept, the computation of entire net income must be made in such manner as the Commissioner of Taxation and Finance deems necessary to properly reflect entire net income."

20 NYCRR 2-2.2 provides:

> "Change of accounting method. (a) If a taxpayer's method of accounting for Federal income tax purposes is changed, the accounting method employed in determining entire net income for purposes of article 9-A of the Tax Law must be changed at the same time to the method approved for Federal income tax purposes. When a change of accounting method occurs, any adjustments which are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted must be taken into account to the extent they are required to be taken into account in determining the taxpayer's Federal taxable income.
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> "(b) A taxpayer whose method of accounting is changed must submit, with its first report in which the new accounting method is used, a copy of the consent of the Commissioner of Internal Revenue, together with complete details of any adjustments with respect to items of income or deduction."

The Division argues that:

> "[w]hile there is no evidence that the I.R.S. made an involuntary change or that the petitioner voluntarily changed the method of accounting for the container deposits, Tax Law s.208.9(d) and 20 NYCRR 3-2.7 give the Division the authority to make such a change regardless of the method utilized for federal purposes" (Division's brief, pp. 16-17).

The Division asserts that:

> "[a] change in accounting method occurs when the overall reporting method changes from one accounting method to another and when a change occurs in the method of reporting any significant item. Treas. Reg. s.1.446-1(e)(2)(ii)(a). (See also, Graff Chevrolet Company v. Campbell, 343 F.2d 568 (Fifth Cir. 1965). Significant items include reserve accounts, accounts payable, accounts receivable and inventory. Treas. Reg. s.1.481-1(b) and Graff, supra at page 571, footnote 5" (Division's brief, p. 10).

The Division asserts:

> "[a] change in accounting methods occurred in [this case] when the Division [on audit] . . .
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> * * *
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> ". . . determined that the unredeemed container deposit receipts reflected on the petitioner's books at the end of f/y/e March 31, 1986 should be included as income for that year. A change of accounting methods requires that adjustments be made to insure that income is not omitted as
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> a result of the change of accounting" (Division's brief, p. 9).

The Division goes on to assert that "[b]ut for the accounting change there would be no tax liability on the container deposit receipts reflected in the f/y/e end of year balances for the closed years" (Division's brief, p. 13).

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20 NYCRR 3-2.8 provides:

> "Taxable year in which income or deduction is included in entire net income. [Tax Law, § 208(9)(d)] In general, the method of accounting used in computing taxable income for Federal income tax purposes is used in computing entire net income. However, whenever the Commissioner deems it necessary in order properly to reflect the entire net income of the taxpayer, the Commissioner may determine the taxable year or period in which any item of income or deduction shall be included, without regard to the method of accounting used by the taxpayer for Federal income tax purposes."

The Division argues that New York State Tax Law § 208(9)(d) is "patterned after, but not identical to the Federal provisions," and that it is appropriate to use Federal case law for guidance (Division's brief, p. 16). Relying on Graff Chevrolet Co. v. Campbell (supra), the Division asserts that the statute of limitations "does not bar the Division from including receipts omitted as a result of the accounting change as income in the year of the change" (Division's brief, p. 15).

In response to the Division's exception, petitioner states that while it "does not contest the authority of the Division to invoke [its] authority under §208.9" (Petitioner's brief, p. 2), Commissioner v. Indianapolis Power & Light Co. (supra) overruled the decision in Dana.

Petitioner also asserts that its:

> "accounting method for Federal income tax purposes was not changed. Such Federal change is a condition precedent to the application of 20 NYCRR 2-2.2. I.R.C. §481 does not apply in the absence of an adjustment pursuant to I.R.C. §446" (Petitioner's brief, p. 2).

Finally, petitioner asserts that:

> "[t]he statute of limitations does bar the Division from including receipts omitted as a result of the accounting change as income in the year of change.
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> "Tax Law §208.9(d) does not incorporate the provisions of I.R.C. §481. Such section merely authorize the Commissioner [of Taxation] '. . . whenever necessary in order properly to reflect the entire net income of any taxpayer, determine the year or period in which any item of income . . . shall be included. . . .' Likewise 20 NYCRR 3-2.7 does not include any provision comparable to I.R.C. §481. All of the illustrations relate solely to correction of the instant period's income. Further, 20 NYCRR 3-2.7(d) clearly indicates that '. . . the Commissioner may determine entire net income solely on the basis of the taxpayer's income during such period'" (Petitioner's brief, pp. 2-3).

We affirm the determination of the Administrative Law Judge.

Initially, we agree, for the reasons put forth by the Administrative Law Judge, that Commissioner v. Indianapolis Power & Light Co. (supra) does not overrule Dana Distribs. v. Commissioner (supra).

We reject, however, the Division's assertion that "[t]he Administrative Law Judge erred in concluding that the statute of limitations bars the Division from taxing container deposits received during the closed years," i.e., 1983, 1984 and 1985 (Division's brief, p. 3).

First, Tax Law § 1083(a) establishes that "three years after a tax return is filed is a sufficiently reasonable time in which the [Division] is to assess a tax" under Article 9-A (Matter of Montauk Improvement v. Procaccino, 50 AD2d 414, 377 NYS2d 795, mod on other grounds 41 NY2d 913, 394 NYS2d 619).

Second, none of the exceptions to the three-year period of limitations spelled out in section 1083(c) are applicable in this case.

Third, we find nothing in the language of Tax Law § 208(9)(d) or the Division's regulations to indicate that the authority granted the Division under section 208(9)(d) may be exercised without regard to the three-year statute of limitations.

We find that the Division's reliance on Graff for the interpretation of section 208(9)(d) is misplaced. In Graff, the Court had to interpret a statute, i.e., section 481, which did not on its face allow the Internal Revenue Service to look into closed years.[7] The Court relied on the legislative history of section 481 which is summarized in the following passage from Grogan v. United States (475 F2d 15):

> [t]he central problem at which Section 481 is directed is the potential over-taxation, under-taxation, or loss (for income tax purposes) of items such as inventories and accounts receivable at the time a taxpayer changes his method of reporting. When a cash-basis taxpayer switches to the accrual basis, for example, the following problem is likely to arise:
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> > "'If in the year of change the taxpayer deducts his opening inventory and does not report as income accounts receivable at

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[7]The Court noted:

> "[t]he only question before us is whether section 481 gives the Commissioner power to tax amounts that should have been reported in closed years. Nothing in the language of the section prevents its application to amounts omitted in the closed years, but nothing in the language expressly authorizes adjustments of such amounts" (Graff Chevrolet Co. v. Campbell, supra).

> the close of the preceding taxable year, [absent some adjustment] there is a double deduction of the inventory to the extent it
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> was paid for and deducted in previous years, and an entire omission from income of the accounts receivable at the close of the last taxable year in which the cash basis was used.'[8]
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> "To meet this problem before Section 481 was enacted in 1954, the Commissioner adopted the practice of granting his consent to a voluntary change in accounting methods only if the taxpayer agreed to transitional adjustments to prevent items from being taxed twice, deducted twice, or omitted altogether (see, e.g., American Automobile Assn. v. United States, 1961 [61-2 USTC ¶ 9517], 367 U.S. 687, 81 S. Ct. 1727, 6 L. Ed. 2d 1109). Following a period of uncertain and inconsistent treatment of cases where the change was not voluntary,[9] the uniform rule emerged that 'when the Commissioner compelled the change in the method of accounting, adjustments could not be required as to prior years.'[10] (E.g., Commissioner v. Dwyer, 2 Cir. 1953 [53-1 USTC ¶ 9320], 203 F.2d 522.)
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> "Specifically taking note of the state of the law as judicially interpreted,[11] the Congress enacted Section 481 of the Internal Revenue Code of 1954" (Grogan v. United States, supra, at 16).

In short, the intent of section 481 was to allow the Commissioner of Internal Revenue to make adjustment for years otherwise closed by the statute of limitations.

The Division does not refer us to, nor does our own research indicate, similar legislative history for section 208(9)(d). In fact, we cannot reconcile the Division's assertion that section 208(9)(d) is "patterned after, but not identical to the Federal provisions," since section 208(9)(d) was enacted in 1944 while section 481 was enacted in 1954. In the absence of such legislative

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8 2 Mertens, Law of Federal Income Taxation § 12.21 at 100.

9 Compare Ross v. Commissioner, 1 Cir. 1948 [48-2 USTC ¶ 9341], 169 F.2d 483, with Fowler Bros. & Cox, Inc. v. Commissioner, 6 Cir. 1943 [43-2 USTC ¶ 9650], 138 F.2d 774. See also, Goodrich v. Commissioner, 8 Cir. 1957 [57-1 USTC ¶ 9608], 243 F.2d 686.

10 Commissioner v. Welch, 5 Cir. 1965 [65-2 USTC ¶ 9450], 345 F.2d 939, 942.

11 See S. FIN. COMM. REP. ON H.R. 8300, 83d Cong., 2d Sess., U.S. Code Congressional & Administrative News at 4696-697 (1954); H.R. Rep. No. 1337, H.R. WAYS & MEANS COMM. REP. ON H.R. 8300, 83d Cong., 2d Sess., U.S. Code Congressional & Administrative News at 4075 (1954).

history, we cannot interpret section 208(9)(d) as authorizing the Division to make adjustments for years otherwise closed by the statute of limitations.

We affirm the determination of the Administrative Law Judge.

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 Boening Bros., Inc. is granted to the extent indicated in conclusion of law "G" of the Administrative Law Judge's determination; and

4. The Division of Taxation is directed to modify the notices of deficiency dated June 14, 1989 in accordance with paragraph "3" above, but such notices are otherwise sustained.

DATED: Troy, New York
December 8, 1994

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

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