STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition of **JAMES AND JUDITH BOYLE** for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Year 1975.	: : : : :	DETERMINATION DTA NO. 813970

Petitioners, James and Judith Boyle, 15 Brayton Road, Scarsdale, New York 10583, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the year 1975.

On January 22, 1996 and January 31, 1996, respectively, petitioners, represented by Hugh Janow, Esq., and the Division of Taxation, represented by Steven U. Teitelbaum, Esq. (Michael J. Glannon, Esq., of counsel), agreed to waive a hearing and have the matter determined on submission of documents. All briefs and documents were due by June 19, 1996. The Division of Taxation filed documents on March 19, 1996. Petitioners filed their brief and documents on April 25, 1996. The Division of Taxation filed its brief on May 30, 1996 and petitioners filed their reply brief on June 19, 1996, which date commenced the six-month period for issuance of this determination.

After review of the entire record submitted, Marilyn Mann Faulkner, Administrative Law Judge, renders the following determination.

ISSUE

Whether under the doctrine of equitable recoupment petitioners can offset a 1975 State tax deficiency by a 1976 overpayment of tax where boththe deficiency and overpayments are based upon Federal changes to petitioners' reported taxes in 1975 and 1976 and where the statute of limitations expired with respect to the 1976 tax refund under Tax Law § 687(c).

FINDINGS OF FACT

1. Petitioners and the Division of Taxation ("Division") signed on April 26, 1996 and April 29, 1996, respectively, a Joint Stipulation as to the facts in this case. These facts have been incorporated into the following findings of fact. Petitioners have also submitted proposed findings of facts which have been incorporated into the following findings of fact unless otherwise indicated.

2. The Internal Revenue Service ("IRS") sent to petitioners a letter, dated August 31, 1983, informing them of adjustments to their 1975, 1976 and 1977 income tax returns with respect to their tax shelter activity. Attached to the letter was the IRS examination report (Forms 4549-A, 886-A, 1040, 4625, 3468, and 870) indicating a disallowance of an ordinary loss of $135,170.00 in 1975 with respect to silver transactions (calls and futures) placed on the London Metal Exchange. In its explanation of the disallowance, the IRS stated the following in Form 886-A:

> "Based on an examination of the 7512 and 7612 silver transactions (calls & futures) placed on the London Metal Exchanged [sic] - the ordinary loss generated has been disallowed per Rev. Ruling 80-324, and 77-185; and Reg. Sec. 1.165-1(b); and step-transaction theory; and substance over form principles, and economic reality principles."

The report also set forth an adjustment for 1976 of $56,094.00 with respect to silver transactions of options and futures indicating that petitioners should not have reported this amount as income. The IRS explained this adjustment as follows:

> "Based on the examination of all silver transactions for 7512 & 7612 of options and futures, which have been determined to lack economic reality, the 1976 silver transactions have been eliminated per Rev. Rulings 77-185, 80-324; Reg. Sec 1.165-1(b)."

3. On August 10, 1984, petitioners signed a settlement agreement (Form 906) with the Internal Revenue Service resolving all Federal income tax liabilities of petitioners for the years 1975 and 1976 with respect to the "gains and losses from the purchase and sale of commodity options and futures contracts through Merrill Lynch . . . ." The settlement agreement was signed by an authorized representative of the Commissioner of Internal Revenue on September 25, 1984.

4. The intent of the settlement agreement was to resolve a dispute as to whether the gains and losses from the purchase and sale of commodity options and futures contracts reported by petitioners on their Federal tax returns may be recognized for Federal income tax purposes. In the agreement, it was stated that petitioners reported in their 1975 Federal tax return a $135,170.00 ordinary loss and reported in their 1976 Federal tax return a $591,097.00 long term gain and $478,909.00 short term loss with respect to the purchase and sale of commodity options and futures contracts completed through Merrill Lynch. Based on these gains and losses, petitioners agreed to a proposed tax deficiency for 1975 and an overassessment of tax for 1976. According to the agreement, petitioners agreed "that the overassessment for 1976 contained in Form 870 . . . will be an offset to any amounts payable as an overassessment for the year 1975 which results from a claim for refund or credit filed for the year 1976 attributable to the aforementioned commodity transaction." Attached to the Joint Stipulation by the parties was Form 870-AD which indicated that the amount of the 1975 Federal income tax deficiency was $68,923.00 and the amount of the 1976 and 1977 Federal income tax overassessment was $10,458.00 and $57.00, respectively.[1]

5. Petitioners did not timely file within 90 days reports of the Federal audit changes (Form IT-115) that resulted from the settlement agreement. Tax Law § 659 requires the taxpayer to report any changes or corrections by the United States Internal Revenue Service to the taxpayer's Federal income tax within 90 days of the final determination of such change or correction.

6. The Division of Taxation issued to petitioners a Notice of Additional Tax Due (assessment number L-005332770), dated March 2, 1992, stating that based on the Federal audit changes, petitioners owed for the 1975 tax year an additional $20,083.71, plus interest in the amount of $51,061.65, for the total amount of $71,145.36. The Division calculated the 1975

[1] In petitioners' proposed finding of fact "2", petitioners state that the Closing Agreement "allowed Taxpayers a reduction of their 1975 tax deficiency from commodities straddle transactions by an amount equal to the overassessment those transactions created in 1976." This proposed finding of fact is not incorporated into the findings of fact because it involves a legal issue in dispute as to whether there is evidence to show that the 1975 and 1976 adjustments emanated from the same commodities straddle transaction.

deficiency without providing offsets, as was permitted in the settlement agreement, for the 1976 overassessment agreed to between petitioners and the IRS in the settlement agreement.

7. The Division issued to petitioners a Notice of Assessment Resolution, dated May 23, 1994, with respect to assessment number L-005332770. In that notice, the Division stated that the balance of $12,623.61 must be paid in full after which time petitioners could file a claim for refund. In calculating the balance of $12,623.61, the Division noted it applied payments and credits in the amount of $62,012.65 to the amount due of $20,083.71, plus $54,251.32 in interest and $301.23 in penalty.

8. Petitioners filed a Report of Federal Changes (IT-115), dated April 15, 1994, for the tax year 1976 indicating a refund due of $3,387.00. Petitioners also filed a Report of Federal Changes (IT-115), dated June 15, 1994, for the tax year 1975 requesting a refund of $13,156.00. They calculated the refund by taking into account their payments of $62,013.00 and $12,623.00 on July 2, 1992 and June 15, 1994, respectively, and a "discounted 1976 refund" of $3,122.00. They subtracted the total amount of the payments plus the discounted 1976 refund from the sum of $20,066.00 (the additional tax due plus interest) and interest in the amount of $44,536.00 to arrive at the $13,156.00 refund.

9. The Division issued a Notice of Disallowance, dated July 26, 1994, denying the refund claim for $13,156.00 on the ground that the claim was not filed within two years and 90 days of the final Federal determination. The Division noted that the refund claim was received on July 15, 1994 and the final Federal determination was dated September 25, 1984. On the top of the notice the tax year listed was 1976.

10. After a conciliation conference on March 10, 1995, the conciliation conferee issued to petitioner James Boyle an order, dated April 28, 1995, sustaining the statutory notice. In the caption of the order, the year specified was 1975 and there was the notation "Notice of Disallowance Dated July 26, 1994".

11. Petitioners filed a petition, dated June 12, 1995, with respect to the tax year 1975 challenging notice/assessment number L-005332770 and stating that the amount contested was

$13,156.00. In the petition, petitioners alleged that on June 10, 1994, petitioners paid the disputed amount and then filed a claim for refund which was disallowed by notice dated July 26, 1994. They also alleged that they requested a Conciliation Conference protesting the Notice of Disallowance and that by Conciliation Order, dated April 28, 1995, the conferee sustained the Notice of Disallowance. Petitioners argued that the Division failed to compute the 1975 State tax deficiency in a manner consistent with the computation of the 1975 deficiency as set forth in the Federal Closing Agreement; that the Division had not audited petitioners' returns and instead based the deficiency on the Federal audit; and that the Division's refusal to follow the terms of the Closing Agreement, which reduced the 1975 deficiency by the 1976 overassessment, constituted an attempt to collect the same tax twice.

12. The Division filed an answer, dated August 21, 1995, admitting that petitioners paid the 1975 deficiency on June 10, 1994 and then filed a claim for refund which was disallowed by the July 26, 1994 Notice of Disallowance. The Division also admitted that the Conciliation Order, dated April 28, 1995, sustained the Notice of Disallowance. In the answer, the Division further stated that it correctly and properly concluded that petitioners had additional taxable income for 1975 based on Federal audit changes to petitioners' 1975 income tax return which were not timely reported to New York State.

13. In a letter dated February 13, 1996, the Administrative Law Judge ("ALJ") informed the parties of the due dates for the submission of all briefs and evidentiary documents in the case. The ALJ noted that the record would be closed as of April 25, 1996 and no further evidence would be admitted after that date.

SUMMARY OF THE PARTIES' POSITIONS

14. Petitioners argue that the Division is bound to accept the audit changes of the Internal Revenue Service when it does not conduct an independent audit or investigation of petitioners' tax deficiency; that the Division's assessment of the 1975 tax deficiency is inconsistent with petitioners' settlement agreement with the IRS in contravention of Tax Law § 659 and 20 NYCRR 159.4; that petitioners and the IRS structured the settlement agreement so

that the overall tax result would accurately reflect petitioners' commodities transactions that straddled two years; that the Division is attempting to exact a double tax for a single transaction by disallowing the loss side of the transaction without providing an offsetting credit for taxes which were paid on straddle gains.

15. The Division argues that this case does not involve an audit matter but instead involves whether Tax Law § 687(c) prevents petitioners from obtaining a refund 10 years after final Federal income tax changes for 1976; that there is no need for it to conduct an audit when the claim for refund was time-barred; that petitioners failed to timely report the Federal changes for 1976 and thereby lost their opportunity to claim a refund for that year; that petitioners had not proved the 1975 and 1976 income tax adjustments by the IRS emanated from the same "straddle losses"; that petitioners' failure to receive a refund for 1976 "does not constitute a 'double taxation' as argued by petitioners"; and that petitioners "took a gamble and lost" when they decided not to inform the Division of the IRS changes to its income taxes for 1975 and 1976, resulting in the increased tax liability for 1975 but no refund for 1976.

16. In their reply brief filed on June 19, 1996, petitioners argue that the Division's brief failed to respond to the issue presented, and instead, incorrectly implied that their refund claim for 1975 was a refund claim for 1976. Petitioners also contend that they carried their burden of showing that the 1975 and 1976 income tax adjustments emanated from the same "straddle losses". Petitioners attached to their reply brief seven exhibits, three of which had already been submitted into the record.

17. By letter dated July 1, 1996, the Division objected to petitioners' submission of the four documents that had not been submitted prior to the closing date of the record on April 25, 1996, and requested that they be excluded from the record.

CONCLUSIONS OF LAW

A. The Division's request to exclude from the record the four documents, which petitioners submitted after the close of the record on April 25, 1996, is granted. As noted above, in a letter dated February 13, 1996, the parties were informed that the record would be closed as of April 25, 1996 and no further evidence would be admitted into the record after that date. This statement mirrors the Tax Appeals Tribunal's long-standing policy of not allowing the submission of evidence after the close of the record (see, Matter of Schoonover, Tax Appeals Tribunal, August 15, 1991). The Tribunal has opined that this policy is essential to maintain a fair and efficient hearing system, to provide definition and finality to the hearing, and to protect the adversary's right to question the evidence on the record (id.).

B. Tax Law § 659 requires a taxpayer to report any changes or corrections by the United States Internal Revenue Service in Federal taxable income to the Division of Taxation within 90 days after the final determination of such change or correction. Tax Law § 687(c) provides that a claim for any credit or refund of any overpayment of tax attributable to a Federal change or correction required to be reported pursuant to section 659, "shall" be filed within two years from the time the notice of the Federal correction or change was required to be filed with the Division of Taxation. The statute further provides that in the event the change is not reported within the 90-day period, the taxpayer is not entitled to any interest on the claim for credit or refund of the overpayment attributable to the Federal change or correction. Section 687(c) also provides that "[t]his subsection shall not affect the time within which or the amount for which a claim for credit or refund may be filed apart from this subsection".

In this case, petitioners did not file a report of the Federal changes with the Division within 90 days and did not file a claim for a credit or refund with respect to the Federal changes within the 2 years and 90 days required under section 687(c). Petitioners argue that the Division's assessment of the 1975 tax deficiency based on the Federal audit without allowing the offset from the 1976 tax year in accordance with the IRS settlement agreement is inconsistent with the Division's regulations -- 20 NYCRR 159.4. That regulation provides that the Division is not required to accept as correct any Federal changes to a taxpayer's Federal taxable income and instead may conduct an independent audit or investigation. Petitioners contend that because the Division did not conduct an independent audit and instead relied on the Federal audit, the Division was bound to follow the Federal treatment of the 1975 tax deficiency by allowing the 1976 offset.

C. Although not specifically referred to by name, petitioners' claim that the Division is attempting to exact a double tax on a single transaction appears to invoke the doctrine of equitable recoupment. The United States Supreme Court articulated the doctrine of equitable recoupment in Bull v. United States (295 US 247, 79 L Ed 1421). In that case, the Federal government determined that the executor of an estate owed an income tax deficiency based upon moneys received by the estate which had been reported by the executor as decedent's interest in a partnership at the time of death. The executor paid the tax and then filed a refund claim alleging that the government should have deducted the amount of estate tax he paid on decedent's partnership interest which the government now claimed to be income. The Government denied the refund request stating that the statute of limitations had expired with respect to the refund of estate tax incorrectly paid. The U.S. Supreme Court reversed this determination and found that the identical money was subject to double taxation because it was the basis for two assessments involving inconsistent legal theories. The Court agreed that the money in question could not constitute both corpus and income of the estate. The Court further held that there was no procedural impediment to the executor's cross-demand for credit because "[i]t is immaterial that in the second case, owing to the summary nature of the remedy, the taxpayer was required to pay the tax and afterwards seek refundment." (Id. at 263.) Thus, the Court held in favor of the executor stating that because the Government brought a new proceeding arising out of the same transaction involved in an earlier proceeding, he was not barred by the statute of limitations. The Court stated:

> "If the claim for income tax deficiency had been the subject of a suit, any counter demand for recoupment of the overpayment of estate tax could have been asserted by way of defense and credit obtained, notwithstanding the statute of limitations had barred an independent suit against the government therefor. This is because recoupment is in the nature of defense arising out of some feature of the transaction upon which the plaintiff's action is grounded. Such a defense is never barred by the statute of limitations so long as the main action itself is timely." (Id. at 262.)

A further review of the subsequent cases applying the doctrine is instructive. The U.S. Supreme Court applied the doctrine of equitable recoupment in favor of the Government in

Stone v. White (301 US 532, 81 L Ed 1265). In that case, the question was whether the Government was barred by the statute of limitations from a setoff of tax owed by the beneficiary of a trust estate against a timely refund request by the testamentary trustees, who erroneously paid tax on the income of the trust estate, which instead should have been paid by the beneficiary. The Court found that because the trustees represented and acted for the beneficiary, no injustice would be done to the trustees or the beneficiary by withholding from the trustees money which in equity was the beneficiary's. In holding in favor of the Government, the Court invoked the doctrine of equitable recoupment and noted as follows:

> "Here the defense is not a counter demand on petitioners, but a denial of their equitable right to undo a payment which, though effected by an erroneous procedure, has resulted in no unjust enrichment to the government, and in no injury to petitioners or their beneficiary. The government, by retaining the tax paid by the trustees, is not reviving a stale claim. Its defense, which inheres in the cause of action is comparable to an equitable recoupment or diminution of petitioners' right to recover. 'Such defense is never barred by the statute of limitations so long as the main action itself is timely.'" (Id. at 539.)

In a subsequent case, the U.S. Supreme Court distinguished Bull v. United States (supra) and Stone v. White (supra) and held that the doctrine of equitable recoupment did not apply to the facts in that case (Rothensies v. Electric Storage Battery Co., 329 US 296, 91 L Ed 296). The taxpayer in Rothensies was a company that paid excise tax from 1919 to 1926 on the sale of storage batteries in the belief that such sales were subject to tax. In 1926, the taxpayer filed a refund claim for part of the taxes which it had paid between 1922 and 1926. The Circuit Court of Appeals, Third Circuit, found in favor of the taxpayer and the amount requested was refunded (63 F2d 715). However, the taxpayer received the refund in 1935 and because it had deducted from income the tax paid from 1922 to 1926, the IRS treated the refund as income for 1935. The taxpayer paid the deficiency for 1935 and then filed a refund requesting that the deficiency be set off by the amount of excise tax it had paid between 1919 and 1922.

In distinguishing the facts in Bull v. United States and Stone v. White from those of Rothensies, the U.S. Supreme Court noted that in Bull and Stone both the claim and recoupment involved a single taxable event and that the single transaction or taxable event had been subjected to two taxes on inconsistent legal theories. The Court also discussed the reason and character of statutes of limitations pointing out that they are designed "to promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared" (Rothensies v. Electric Storage Battery Co., supra, at 301). The Court further noted that even if one had a just claim, the adversary's right to be free of stale claims should prevail. The Court therefore concluded that applying the doctrine of recoupment under the facts of the case would seriously undermine the statute of limitations in tax matters inasmuch as "[e]very assessment of deficiency and each claim for refund would invite a search of the taxpayer's entire tax history for items to recoup" (id. at 302).

The U.S. Supreme Court also declined to apply the doctrine of equitable recoupment in a case where the taxpayer had litigated a tax liability in Tax Court without raising an equitable recoupment claim and then sought recoupment in a separate action for refund that had been barred by the statute of limitations (United States v. Dalm, 494 US 596, 108 L Ed 2d 548).

The Tax Appeals Tribunal has similarly declined to apply the doctrine of equitable recoupment in a case noting that "credit for overpayment of taxes in a previous year which is barred by the statute of limitations may not be recouped against taxes due for a different year on different transactions not under audit" (Matter of Kadish, Tax Appeals Tribunal, November 15, 1990, citing Matter of Mobil Oil Corp. v. State Tax Commn., 62 AD2d 668, 406 NYS2d 365).

D. In the current case, the first issue under the recoupment doctrine is whether petitioners are litigating the recoupment in the 1975 tax deficiency proceeding or in a separate proceeding for refund which is time barred. The Division appears to claim that petitioners are seeking an offset to their tax deficiency in a separate refund claim for 1976 whereas petitioners assert that they paid the 1975 deficiency and then filed a timely refund claim with respect to the 1975 deficiency raising the defense of an offset for overpayments in 1976.

In contrast to the situation in United States v. Dalm (supra), the record shows that petitioners litigated the 1976 offset issue in a proceeding concerning the Division's 1975 deficiency claim. In the Notice of Assessment Resolution, dated May 23, 1994, it was stated that petitioners must pay the balance of the $12,623.61 owed on the 1975 deficiency after which they could file a claim for refund. Petitioners alleged in their petition that they had paid the 1975 deficiency on June 10, 1994 and then filed a claim for refund which was denied in the Notice of Disallowance dated July 26, 1994. They also alleged that they then requested a Conciliation Conference protesting the Notice of Disallowance. In its answer, the Division admitted the truth of those allegations, therefore, they are accepted as facts. Although the Notice of Disallowance, dated July 26, 1994, listed the tax year as 1976, the Conciliation Order that sustained the Notice of Disallowance stated that the tax year in question was 1975. Given the sequence of events and the reference to the 1975 tax year in the Notice of Assessment Resolution and the Conciliation Order, it appears that the Notice of Disallowance incorrectly listed the tax year as 1976. Thus, unlike the situation in Dalm, the doctrine of equitable recoupment should not be rejected on the ground that the doctrine was raised in a proceeding that was untimely commenced inasmuch as petitioners raised the 1976 offset as a defense in the 1975 tax deficiency proceeding.

E. The next threshold question is whether the deficiency and offset involve a single taxable event. The Tax Appeals Tribunal recently set forth the criteria for the application of the doctrine of equitable recoupment in Matter of Turbodyne (Tax Appeals Tribunal, July 3, 1996). The Tribunal stated that:

> "[t]he doctrine of equitable recoupment allows a taxpayer against whom a deficiency is asserted to offset against that deficiency overpayments which are time barred for claiming a refund and (1) involve the same type of tax as the deficiency; (2) were paid during the period that comprises the deficiency; and (3) involve the same transaction as is the subject of the deficiency. . . ."

The Division claims that petitioners have not shown that the deficiency and offset involve the same straddle transactions. However, a comparison of the terms of the settlement agreement and the IRS examination report accompanying the August 31, 1983 letter to petitioners informing them of the adjustments to their 1975, 1976 and 1977 income tax returns, indicates that the 1975 deficiency and 1976 offset involve the same straddle transactions with respect to silver options and futures. The settlement agreement shows that petitioners reported a $135,170.00 loss in 1975 and a $591,097.00 long term gain and a $478,909.00 short term loss in 1976 with respect to the purchase and sale of commodity options and futures contracts. Subtracting the short term loss from the long term gain in 1976 results in a gain of $112,188.00. The IRS examination report states that the IRS was disallowing the $135,170.00 loss in 1975 and making an adjustment in 1976 by disregarding the $56,094.00 as income, which amount reflects 50% of the $112,188.00 gain reported by petitioners in 1976. The IRS explanation on Form 886-A clearly indicates that the adjustments for 1975 and 1976 were based on the same silver transactions of options and futures (see, Finding of Fact "2").

Petitioners assert that these silver transactions are straddle transactions.

> "A 'straddle' is a combination of a sale contract and a purchase contract undertaken at the same time. . . . [T]he sale and purchase would differ in their delivery dates so that a straddle would typically result in a present agreement to purchase (or sell) a commodity at a future date and sell (or purchase) the same commodity at a later date. As the prices of the commodity and of the contracts change, they will, of course, cause a gain and loss in any contract position . . . . [and] any gain or loss in one of the positions will be offset by an opposite change, hopefully equal, in the other position" (Matter of Hemmers, Tax Appeals Tribunal, March 1, 1990).

Based on the record, petitioners have shown that the 1976 overpayment involves the same tax and the same transactions as the 1975 deficiency.

F. The remaining question is whether the 1976 overpayment was paid during the period that comprises the 1975 deficiency for purposes of the application of the doctrine of equitable recoupment. In Matter of Hemmers (supra), the Tribunal held that it was precluded by Tax Law § 689(g) from determining whether there was an overpayment in a year that was not in issue, thus eliminating the application of the doctrine of recoupment. However, the facts in this case are distinguishable from those in Hemmers. In this case, the Division's calculation of the 1975 deficiency was based on the IRS audit of petitioners' income tax returns for 1975, 1976 and 1977. The Division chose, however, to base the State 1975 deficiency on the IRS' adjustments for 1975 without the offset allowed by the IRS due to its finding of overpayments by petitioners in 1976. As noted by petitioners, the Division was permitted under the regulations not to accept as correct the results of the IRS audit, and instead, to conduct an independent investigation (20

NYCRR 159.4). However, the Division did not conduct an independent investigation and accepted as correct the IRS determination of the amount of the 1975 deficiency. Thus, inasmuch as the Division based its 1975 deficiency on the IRS audit, it would be inconsistent to ignore the terms of the IRS settlement agreement for those audited years which reduced that 1975 deficiency by the 1976 overpayment. Unlike the situation in Matter of Hemmers (supra), the Division based its 1975 deficiency exclusively on an IRS audit of the same transactions with respect to the silver options and futures which spanned both 1975 and 1976. Therefore, the 1976 overpayment comprises the same period as the 1975 deficiency for purposes of the doctrine of equitable recoupment (see, Matter of Mobil Oil Corp. v. State Tax Commission , 62 AD2d 668, 406 NYS2d 365; National Cash Register Co. v. Joseph, 299 NY 200).

G. Based on the case law, there is no indication that the doctrine of equitable estoppel should not be applied to the facts and circumstances in this case. The doctrine is based on principles of fairness. It would be unfair for the Division to select only those parts of the IRS audit that result in a tax deficiency without considering the IRS finding of overpayments of tax on the same options and futures transactions. Similar to the situation in Stone v. White (supra), the purpose of the statute of limitations in Tax Law § 687(c) would not be undermined by the application of the doctrine of equitable recoupment in this case. Thus, petitioners should be allowed to offset the 1975 deficiency by the amount of the 1976 overpayment which results from incorporating the findings of the IRS audit of petitioners' 1976 Federal return as finally set forth in the settlement agreement.

H. In its brief, the Division implies that because petitioners failed to report the IRS changes within 90 days, petitioners took a gamble that the Division would consider both the 1976 overpayment along with the 1975 deficiency when it discovered the IRS changes. The Division contends that petitioners lost this gamble and therefore are not entitled to any offset as a result of their conduct. This result is not required by the statute. According to Tax Law § 687(c), because petitioners failed to report to the State the Federal changes to their Federal taxes within 90 days, they are not entitled to any interest on any offset of the 1976 overpayment attributable to the Federal changes. Thus, to the extent petitioners have included interest on the overpayment in calculating their offset, it is not allowed.[2]

I. The petition of James and Judith Boyle is granted to the extent indicated in Conclusions of Law "G" and "H" and is otherwise denied.

DATED: Troy, New York
December 12, 1996

/s/ Marilyn Mann Faulkner
ADMINISTRATIVE LAW JUDGE

[2]In their Report of Federal Changes (Form IT-115) for 1975, petitioners subtracted from the additional tax due a "discounted 1976 refund" of $3,122.00. It is unclear how this amount was calculated.