STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
GOETZ ENERGY CORPORATION	:	DETERMINATION DTA NO. 815558
for Redetermination of a Deficiency or for Refund of Corporation Tax under Article 9 of the Tax Law for the Years 1991 through 1993.	:	

Petitioner, Goetz Energy Corporation, P.O Box A, Buffalo, New York 14217-0305, filed a petition for redetermination of a deficiency or for refund of corporation tax under Article 9 of the Tax Law for the years 1991 through 1993.

A hearing was held before Timothy J. Alston, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on September 9, 1997 at 1:00 P.M., with all briefs to be submitted by January 20, 1998, which date began the six-month period for the issuance of this determination. Petitioner appeared by Gary M. Kanaley, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Laura J. Witkowski, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly denied petitioner's claim for refund of tax paid pursuant to Tax Law § 186-a for the years 1991 through 1993 where, following petitioner's payment of such tax, the Division agreed not to audit or assess certain other taxpayers for potential liabilities arising under section 186-a for years prior to 1994.

FINDINGS OF FACT

1. Petitioner, Goetz Energy Corporation, is a petroleum distributor that sold and marketed natural gas through pipes and mains in New York State for ultimate consumption within the State during the years 1987 through 1994.

2. Petitioner was subject to tax under Tax Law § 186-a during 1987 through 1994 because of its activities as a seller and marketer of natural gas.

3. Petitioner, along with other companies in the natural gas industry, did not timely file returns and pay tax due under Tax Law § 186-a of the Tax Law for the years 1987 through 1993 because of confusion as to its liability.

4. In January 1994, attorney Mark Klein of the Buffalo law firm of Hodgson, Russ, Andrews, Woods & Goodyear requested and was granted a meeting with the Director of the Corporation Tax Bureau, Dominick Sciortino. At this meeting, Mr. Klein informed the Division that he represented a taxpayer who had not been properly filing under Tax Law Article 9, § 186-a, but who now wanted to come forward and file returns. The identity of the taxpayer in question, although not revealed to the Division at that time, was the petitioner in this matter.

5. Mr. Klein proposed that his client would file returns and pay the tax due under section 186-a for the years 1991 through 1993. In return for the taxpayer's voluntary compliance, Mr. Klein requested that the Division not assess penalties or audit or assess the taxpayer for years prior to 1991.

6. As a follow-up to the January 1994 meeting, Mr. Klein sent a letter to the Division which reiterated the background facts and confirmed that an agreement had been reached. The substance of the agreement was that the taxpayer would come forward and file returns for the previous three years and the Division would accept such returns as filed and not assess penalties with respect to the 1991 and 1992 returns. In addition, the Division agreed to limit petitioner's

exposure to the section 186-a tax to tax years beginning after December 31, 1990. The Division was unwilling to put this agreement in writing; however, the Division did agree to the terms proposed and accepted the returns and payments subsequently remitted by petitioner.

7. Petitioner filed forms CT-186-A for the years 1991 through 1993 on or about March 8, 1994. These returns reported tax due under section 186-a in the respective amounts of $37,549.88 (1991), $64,821.77 (1992), and $81,531.60 (1993). Payment in full of the tax reported due accompanied the returns.

8. Petitioner received a financial benefit as a result of the Division's agreement not to assess penalties with respect to its 1991and 1992 returns and not to audit or assess petitioner for years prior to 1991. There is insufficient information in the record regarding the nature of petitioner's business before 1991 to reasonably estimate the amount of this benefit.

9. The Division accepted petitioner's returns for the years at issue as filed. The Division did not audit petitioner with respect to Tax Law § 186-a for any of the years during which petitioner was engaged in the business of selling and marketing natural gas.

10. On or about May 22, 1996, petitioner filed three claims for credit or refund of corporation tax paid (Form CT-8) and amended utility services tax returns (Forms CT-186-A) for the years ended 1991 through 1993. These documents claimed refunds of the amounts of tax under section 186-a previously paid on or about March 8, 1994 (***see***, Finding of Fact "7").

11. The basis for petitioner's refund claims was a January 10, 1995 letter that had been sent by John B. Langer, former Deputy Commissioner for Operations, to Mark Klein (in his capacity as representative for other gas marketers), wherein the Division indicated that for the companies who voluntarily came forward, properly filed and (where appropriate) paid their

section 186-a tax liabilities for the 1994 tax year forward, the Division would not go back and audit prior tax years.

12. On August 24, 1995, the Division issued to petitioner a Notice of Disallowance covering all three refund claims. The Notice of Disallowance stated that petitioner was correctly classified as an Article 9, section 186-a taxpayer and that it had properly filed returns for the 1991 through 1993 period. Accordingly, the notice stated that there was no basis for the refund claims.

13. On December 1, 1994, following the negotiation of the agreement between petitioner and the Division and petitioner's filing of returns and payment of section 186-a tax, the Division met with Mr. Klein, along with a lobbyist for the Independent Oil and Gas Association of New York (IOGA) and the president of a gas marketing company headquartered outside of New York. One of the issues to be discussed at the meeting was the alleged confusion in the natural gas industry regarding which taxpayers were subject to section 186-a. It is not clear whether Mr. Klein was representing IOGA, the out-of-state based marketer or other gas marketers at this meeting.

14. The Division was advised at the meeting that there were a number of gas marketers who should have been filing and paying tax under section 186-a, and that these noncompliant marketers wanted to correct the situation.

15. When a taxpayer voluntarily discloses a failure to file returns the Division's general policy is to request that the taxpayer submit a letter setting forth the facts of its situation and stating how the taxpayer would like to proceed. The method by which the Division ultimately resolves the situation varies from case to case. Depending upon the facts, the Division may require the taxpayer to file returns from the date it began doing business; require the taxpayer to

file returns for a number of years (e.g., 1 to 3 years); or it may require the taxpayer to file for the current tax year and forego any audits of prior years. The Division tries to be consistent, but does not treat all voluntary disclosures in the same industry in the same manner.

16. According to John Verde, Tax Administrator I, one of the reasons for the Division's inconsistency in handling voluntary disclosures is that it must rely on the facts as presented by the taxpayer's representative and the Division generally is not advised of the identity of the taxpayer in question until it agrees to the terms proposed by the representative.

17. The issue of companies which had already come forward and paid tax due under section 186-a for prior years was discussed at the meeting. Mr. Klein advised the Division not to worry about those taxpayers and that the main concern at that point was a level playing field from that time forward. The Division's original position was that the taxpayers under consideration should file returns and pay tax due for the previous three years. However, the taxpayer group indicated that the companies in question were poor farmers who would be forced out of business if they were required to pay retroactively.

18. There is no evidence in the record that petitioner ever consented to the settlement agreement reached with the other companies or that such other companies were actually concerned about leveling the playing field for the future.

19. The Division's former Deputy Commissioner for Operations, John B. Langer, subsequently sent a letter to Mr. Klein, dated January 10, 1995, to confirm the settlement reached as a result of the foregoing discussion. That letter provides, in pertinent part:

> On December 1, 1994 we met with you and several other persons concerning the application of sections 186 and 186-a of the Tax Law to gas producers, sellers and marketers. You concurred with other persons from the industry attending this meeting (as well as an earlier meeting) that there had been significant confusion among many people in the natural gas distribution industry

> about their functions as 'sellers' or 'marketers' in the natural gas distribution system. . . . You advised that some well-counseled firms in the industry had, notwithstanding this confusion, met their legitimate Article 9 state tax obligations and were most concerned about 'leveling the playing field' for the future rather than the perceptions of past 'inequities'.
>
> Subsequently, you and others were advised that the Department acknowledged that the confused state of affairs within the industry and the strong desire of those who would have paid their apparent Article 9 state tax obligations to begin filing and paying appropriately for 1994, required us to rethink our audit program in this area. Specifically, we have advised that with respect to companies which voluntarily come forward, properly file, and, where appropriate, pay their Article 9 tax liabilities (generally arising under sections 186 and 186-a) beginning with tax year 1994 and all subsequent periods, we will eschew our authority to audit such companies for potentially similar liabilities for pre-1994 tax periods. Obviously, companies who do not desire to meet their tax obligations by coming forward as proposed cannot claim 'good faith' uncertainty as to any of their obligations (now or before) and will be subject to audit.
>
> We confess to some confusion as to your questions about refund claims in light of your statements about the appropriate and careful tax advice which had been afforded to certain companies within this industry that they were obliged to make filings and payments pursuant to Article 9. If tax liabilities were due, owing and appropriately paid, obviously, 'refund' claims will be denied. You are, of course, fully conversant with available remedies when claims of overpayment are denied by the Department.

20. At the hearing, Mr. Verde, who was present at the meeting and involved in the Division's handling of this matter, testified as to the intent of the Division in issuing the January 10, 1995 letter. According to Mr. Verde, the Division sought to comply with the taxpayers' request to level the playing field for the future. Also according to Mr. Verde, the Division's decision to "eschew" its authority to audit for pre-1994 liabilities with respect to companies who came forward and began to file for 1994 was justified because the Division did not know the identities of the companies involved, had no formal audit program in this area and no means of finding every nonfiler. The Division therefore decided to proceed in the manner described in the

letter in an effort to bring taxpayers into compliance as of the current year and thereby prevent future inequities.

21. The Division also concluded that factual differences existed between petitioner's situation and the situation of the noncompliant taxpayers described at the meeting which warranted its acceptance of the settlement terms proposed at the meeting. Specifically, the noncompliant taxpayers described at the meeting were said to be small, unsophisticated farmers who would be forced out of business if required to pay tax owed under section 186-a for prior years. In contrast, the Division perceived petitioner to be a large, sophisticated corporation with the resources to pay past due taxes.

22. The Division received Article 9, § 186-a returns from three or four taxpayers in response to the policy stated in the January 10, 1995 letter. These three or four taxpayers were large companies headquartered in other states. According to Mr. Verde, these companies were larger than the Division had anticipated based on the discussions at the meeting. Overall, the Division detected no significant increase in the number of Article 9, § 186-a returns filed for the 1994 tax year, as compared to the previous year.

23. Following receipt of petitioner's refund claims in May 1995, the Division concluded that there had been a misunderstanding of the settlement terms by Mr. Klein. It was the Division's position that the January 10, 1995 letter had clearly stated that refunds of tax properly paid would not be made. Nonetheless, at least one of Mr. Klein's clients, i.e., petitioner, who had late-filed and paid the tax due, had subsequently filed a refund claim. Since the Division had not expected to receive such a refund claim, and in order to make the Division's position clear, the acting Deputy Commissioner of Operations, Harris Sitrin, sent a letter to Mr. Klein, dated March 12, 1996, which stated, in pertinent part:

> As you recall, the [January 10, 1995] correspondence provided the opportunity for those companies subject to the [§ 186-a] tax to come forward and properly address their Article 9 tax liability for 1994 and future years. To date, several companies have come forward to address their filing responsibility.
>
> To assure that the Department's position is the proper position required by law, I have sought the advice of Counsel. That advice is stated as follows:
>
> 1. The Commissioner or his delegate does have the power to encourage non-compliant taxpayers to come forward and pay taxes due and comply with the law, equally;
>
> 2. The audit selection process is the prerogative of the Commissioner. Simply put, the taxpayers and the periods selected are solely at his discretion;
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> 3. The Commissioner's power to promote voluntary compliance should not be misconstrued as a forgiveness of past liabilities of taxpayers who properly paid tax;
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> 4. The law is clear that properly paid taxes cannot be refunded; and
>
> 5. This position was adequately clear in the January 10, 1995 letter, and any refund claims based on past properly paid taxes must be denied.
>
> To eliminate any perceived misconceptions, the portion of the letter, not consonant with the Counsel's opinion, is withdrawn. All entities and persons liable for the tax are subject to the regular audit and selection processes of the Department.

24. According to Mr. Verde, the March 12, 1996 letter was intended to clarify the Division's position with respect to refund claims under the circumstances discussed therein and also to refine the Division's audit policy in this area by clearly stating that all entities and persons liable for the section 186-a tax are subject to the regular audit and selection process.

25. The Division has never audited either petitioner or any of the three or four companies which came forward in response to the policy stated in the January 10, 1995 letter.

26. The Division submitted proposed findings of fact numbered "1" through "30". Of these, proposed findings of fact "1" through "7", "9" through "23", and "25" through "29" are

accepted and have been incorporated, in substance, into the Findings of Fact herein. Proposed finding of fact "8" is rejected because there is insufficient evidence in the record to establish the amount of financial benefit to petitioner as a result of its agreement with the Division (***see***, Finding of Fact "8"). Proposed finding of fact "30" is rejected as irrelevant.

27. In its reply brief, petitioner requested changes in the Division's proposed findings of fact. Of these, the changes proposed by petitioner with respect to the Division's proposed findings of fact "2", "3", "8", "13", "20", "22", and "27" are accepted and have been incorporated into the Findings of Fact herein.

SUMMARY OF THE PARTIES' POSITIONS

28. Petitioner conceded that it reported and paid the proper amount of tax due under Tax Law § 186-a for the years 1991 through 1993. Petitioner also conceded that it was within the Division's authority and discretion to enter into voluntary disclosure agreements such as the agreement between petitioner and the Division and the agreement summarized in the January 10, 1995 letter (***see***, Tax Law § 171[2], [18], [20]). Additionally, petitioner did not question the legitimacy or propriety of either agreement. Rather, petitioner contended that the denial of its refund claim following the Division's decision not to audit natural gas distributors and marketers who voluntarily came forward for the 1994 tax year violated principles of fairness and equity which require the Division to treat similarly situated taxpayers the same.

29. Petitioner further contended that the Division's decision not to audit certain other natural gas distributors and marketers for tax years prior to 1994 and its subsequent denial of petitioner's refund claim for the years 1991 through 1993 violated the equal protection clauses of the New York State and Federal constitutions because such actions arbitrarily distinguish between similarly situated taxpayers and are not rationally related to a legitimate state purpose.

30. The Division asserted that petitioner was not similarly situated to those taxpayers intended to be or actually covered by the Division's January 10, 1995 letter; that petitioner was not treated differently than such taxpayers; and that, even if the Division did treat similarly situated taxpayers differently, the Division had a rational basis for its actions and the treatment was not so disparate as to constitute "invidious" discrimination.

CONCLUSIONS OF LAW

A. As a general principle, "fairness and policy considerations embodied in administrative law demand that agencies treat similarly situated parties consistently. . . [unless] a reasonable explanation for disparate treatment is stated by the reviewing agency" (***Matter of Balan Printing***, Tax Appeals Tribunal, April 17, 1991).

In this case, it is clear that petitioner and the companies who benefitted from the agreement summarized in the Division's January 10, 1995 letter were similarly situated. "An essential element of similarity is whether the taxpayers have been assessed for the same thing" (***id.***). Both petitioner and the taxpayers who came forward in response to the January 10, 1995 letter were natural gas sellers and marketers subject to tax under Tax Law § 186-a.[1] Moreover, notwithstanding testimony presented at hearing by the Division regarding the intent of the letter, the letter itself simply refers to "companies which voluntarily come forward. . . ." The letter thus extended the Division's agreement not to audit for pre-1994 liabilities to all companies that voluntarily came forward and filed under Tax Law § 186-a beginning with the 1994 tax year. Under these circumstances, the question of whether petitioner and these other taxpayers were similarly situated is resolved by the fact that they were equally obligated under Tax Law § 186-a.

[1]Section 186-a of the Tax Law imposes a tax upon the gross income of every utility doing business in New York.

It is also clear that petitioner received different treatment from the Division than the taxpayers that came forward in response to the January 10, 1995 letter. Petitioner's settlement agreement required that petitioner file and pay section 186-a tax for the years 1991 through 1993 in exchange for the Division's agreement not to assess penalties for the years 1991 or 1992 and not to audit or assess petitioner for years prior to 1991. In contrast, the companies that came forward in response to the letter were required to properly file and pay their section 186-a liabilities beginning with tax year 1994 and all subsequent periods in exchange for the Division's agreement not to audit such taxpayers for similar liabilities for pre-1994 periods. Clearly, the taxpayers who came forward in response to the letter got a better deal than petitioner.

The Division asserted that it had consistently treated petitioner and the taxpayers who came forward under the terms of the January 10, 1995 letter because no audits have been conducted for any taxpayer subject to tax under section 186-a. This argument misses the point. As petitioner correctly notes in its brief, this dispute does not center around audit treatment, but tax treatment. Specifically, petitioner paid tax for the years 1991 through 1993 while other taxpayers were effectively relieved of their liability for the same years.

Although the record shows that the Division treated similarly situated parties differently, petitioner's refund claim must be denied because the Division's denial was rationally related to the legitimate State interest of enforcing the Tax Law. "Public policy favors full and uninhibited enforcement of the Tax Law" (***Turner Construction Co. v. State Tax Comm.***, 57 AD2d 201, 394 NYS2d 78, 80). Petitioner seeks a refund of taxes it properly paid pursuant to the relevant statute. It would clearly be against public policy to require the Division to grant petitioner's refund and thereby waive its right to collect taxes lawfully due. Such a result would also run contrary to the general rule, particularly applicable in connection with tax matters, that

laches, waiver or estoppel may not be employed against the State (***Matter of Jamestown Lodge 1681 Loyal Order of Moose [Catherwood]***, 31 AD2d 981, 297 NYS2d 775, 776).[2]

On brief, the Division argued that its decision to agree to the terms of the voluntary disclosure agreement summarized in the January 10, 1995 letter was rationally related to its legitimate goal of maximizing tax compliance. According to the Division, any disparate treatment accorded petitioner was reasonable under these circumstances. As petitioner correctly noted in its brief, however, the Division's argument justifying its decision to enter into this agreement is irrelevant because petitioner does not take issue with the legitimacy of this voluntary disclosure agreement or that it was rationally related to the legitimate goal of obtaining maximum compliance with the Tax Law. Rather, petitioner argued that the denial of its refund claim was arbitrary and not rationally related to the goal of obtaining maximum compliance.

Petitioner is correct on this point, because the denial of its refund claim was unrelated to the Division's interest in maximizing compliance. However, as discussed above, the refund denial was related to the Division's enforcement interest, and therefore was proper.

B. As the Division correctly asserted in its brief, the equal protection issue raised by petitioner amounts to a claim of discriminatory enforcement. That is, petitioner complains that the Division of Taxation enforced Tax Law § 186-a against it with respect to the years 1991 through 1993, but did not enforce the tax imposed under that section for those years against the companies that came forward in response to the letter.

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[2]Ironically, a determination in favor of petitioner herein would likely adversely affect the administration of the Tax Law to the detriment of the general taxpaying public. If the Division were required to refund taxes lawfully paid based on the terms of a later settlement agreement with other taxpayers, its ability to enter into such agreements would be significantly compromised. This would likely result in fewer agreements and less flexibility in the administration of the Tax Law. Under such circumstances, "the balance between administrative flexibility and possible unfairness to a taxpayer weighs in favor of the public interest in enforcement of the Tax Law" (***American Tel. & Tel. Co. v. State Tax Comm.***, 61 NY2d 393, 405, 474 NYS2d 434, 440).

To establish a claim of discriminatory enforcement, petitioner must prove not only selectivity in enforcement, but also that the selectivity "arose from an intentional invidious plan of discrimination on the part of the Division" (***Matter of Petro Enterprises***, Tax Appeals Tribunal, September 19, 1991). "It is only where the party affected can show a palpable and deliberate scheme to oppress him while excluding all others who come within the terms of the [statute] that such an objection (unconstitutionality) can be sustained." (***People v. Dahlman*** 82 Misc 2d 927, 371 NYS2d 60, 63, ***affd*** 87 Misc 2d 261, 383 NYS2d 946 [citations omitted].) Petitioner has clearly failed to make such a showing. Indeed, notwithstanding the denial of its refund claim, petitioner has failed to show that it was singled out for enforcement at all, much less the target of an intentional invidious plan of discrimination. There is no evidence in the record indicating that the Division failed to enforce Tax Law § 186-a for the years 1991 through 1993 except with respect to those who responded to the January 10, 1995 letter.[3] Petitioner was thus simply expected to comply with section 186-a, along with other natural gas sellers in New York during 1991 through 1993, and the Division of Taxation was simply enforcing the Tax Law. Furthermore, even if one were to focus on the difference between petitioner's voluntary disclosure agreement and the voluntary disclosure agreement summarized in the January 10, 1995 letter, it is clear that such difference resulted from a Division enforcement strategy. "[L]atitude must be accorded authorities charged with making decisions related to legitimate law enforcement interests, at times permitting them to proceed with an unequal hand" (***303 West 42nd***

[3]Petitioner incorrectly argued that the Division's action in agreeing to the voluntary disclosure agreement summarized in the letter and its subsequent denial of petitioner's refund claim was to separate similarly situated taxpayers into two groups: (1) those who paid their section 186-a taxes and were denied a refund and (2) those who did not pay their appropriate tax liability. However, as petitioner correctly argued in its brief, and as discussed previously herein, the key to similarly situated status in this case is equality of obligation. Accordingly, the Division's action may be seen as dividing taxpayers into (1) those that did not pay their appropriate section 186-a tax liability for the years 1991 through 1993 and (2) those that did. When viewed in this manner, it is clear that petitioner was not singled out in any way.

St. Corp. v. Klein, 46 NY2d 686, 694, 416 NYS2d 219, 224). In this case, the Division became aware that "there were a number of [noncompliant] gas marketers" (***see***, Finding of Fact "14") and accepted the proposal presented by these taxpayers in an effort to bring them into compliance as of the current year (***see***, Finding of Fact "20"). Without passing on the soundness of the Division's strategy, considering its legitimate interest in maximizing compliance, this exercise of discretionary authority does not support a selective enforcement claim. Indeed, one would be hard pressed to find an invidious plan of discrimination where, as here, the Division consented to settlement terms proposed by the taxpayer, and thereby agreed not to assert liability against the taxpayer with respect to 1987 through 1990 and not to assess penalties against the taxpayer for the years 1991 and 1992.

In its reply brief, petitioner asserted that it was not protesting the nonenforcement of Tax Law § 186-a, but the denial of its refund claim. Petitioner claimed that this action resulted in a denial of its equal protection rights. Therefore, the standard applicable in nonenforcement cases should not apply. This assertion is rejected. While petitioner does protest the denial of its refund claim, that claim is premised on the Division's nonenforcement of Tax Law § 186-a against others during the years 1991 through 1993 while it enforced this section against petitioner during the same period. Thus, the constitutional issue is properly framed as one of discriminatory enforcement.[4]

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[4]Equal protection and discriminatory enforcement are closely related concepts. Indeed, the right to equal protection underlies any claim of discriminatory enforcement (***see, 303 West 42nd St. Corp. v. Klein, supra***, at 693, 416 NYS2d at 223). Moreover, the discriminatory enforcement standard outlined above is similar to the equal protection standard set forth by petitioner in its brief. That standard provides that where, as here, the government's action does not implicate either a fundamental right or a suspect class, equal protection requires only that the government's uneven treatment be rationally related to the achievement of a legitimate government objective (***see, Matter of Balan Printing, supra***). A denial of equal protection under such circumstances will arise only where the uneven treatment is "palpably arbitrary" or amounts to an "invidious discrimination" (***Trump v. Chu,*** 65 NY2d 20, 25, 489 NYS2d 455, 459). Petitioner's constitutional claim also fails under this standard. Specifically, as discussed previously in this determination, the Division's uneven treatment was rationally related to a legitimate State purpose

C. The petition of Goetz Energy Corporation is denied.

DATED: Troy, New York
June 18, 1998

/s/ *Timothy J. Alston*
ADMINISTRATIVE LAW JUDGE

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and, as discussed above, there is no proof of invidious discrimination in this matter.