

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

JAMES H. AND EMILY M. SCHEUER

DECISION

for Redetermination of a Deficiency or for
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Year 1972.

Petitioners, James H. and Emily M. Scheuer, c/o Oppenheim, Appel, Dixon & Co., 101 Park Avenue, New York, New York 10178, 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 1972 (File No. 24288).

A hearing was commenced before Robert A. Couze, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on April 23, 1982 at 2:00 P.M. and continued to conclusion before Doris E. Steinhardt, Hearing Officer, on June 5, 1985 at 9:15 A.M., with **all** briefs to be submitted by September 25, 1985. Petitioners appeared by Oppenheim, Appel, Dixon & Co. (Jack Wong, CPA). The Audit Division appeared by John P. Dugan, Esq. (Anne W. Murphy, Esq., of counsel).

ISSUES

I. Whether petitioners properly considered the modification to the item of tax preference for capital gains required by Tax Law section 622(b)(4) to be equivalent in amount to the capital gain modification to federal adjusted gross income required by section 612(b)(11).

II. Whether petitioners were entitled to carry back to 1972 a net operating loss of \$77,956.00 incurred in 1975.

FINDINGS OF FACT

1. For the taxable year 1972, petitioners, James H. and Emily M. Scheuer, filed a joint federal income tax return and a joint New York State income tax resident return, reporting income in the categories and amounts shown below.

Wages:	
U.S. House of Representatives, net of expenses (H)	\$ 23,509
Renewal & Development Mgt. Co. (H)	11,343
District Furniture Corp. (H)	3,000
Emily Malino Assoc. (W)	<u>13,505</u>
Total Wages	51,357
Dividends net of exclusion	219,024
Interest income	14,329
Business income (Schedule C)	(277,978)
Capital gains less I.R.C. section 1202 deduction of \$560,415	526,591
Income from rent, partnerships and trusts	(234,254)
Other income	<u>(295,446)</u>
Total adjusted gross income	39,623
Less itemized deductions	<u>39,623</u>
	-0-
Less exemptions	<u>4,500</u>
Taxable income (loss)	<u>(4,500)</u>

The loss in the amount of \$295,446.00 reported as "other income" was calculated as follows:

Gilbert & Gilbert - consulting fee (H)	\$ 20,000
Washington Post - consulting fee (W)	75
CP 5 Inc. - Income recognized on liquidation of assets under I.R.C. section 3.33	170,349
Miscellaneous income	<u>415</u>
Balance	\$190,839

Less: net operating loss carryforwards

1967	\$128,303	
1968	87,839	
1969	188,870	
1970	200,609	
1971	<u>78,338</u>	
Total NOL	\$683,959	
NOL applied to reduce taxable income to zero	(486,285)	(486,285)
NOL to be applied against section 1202 deduction	107,674	

Petitioners also reported the following federal items of tax preference:

Accelerated depreciation		\$ 3,084
Capital gains, section 1202 deduction	560,415	
Less: NOL carryforward	(197,674)	
Net capital gains, section 1202 deduction		<u>362,741</u>
Federal items of tax preference		<u>\$365,825</u>

2. On November 12, 1975, petitioners filed a refund claim with the Internal Revenue Service, seeking to carry back to the year 1972 a net operating loss of \$189,609.00 incurred in 1973. The loss was applied against the tax preference income of 1972, as shown below, resulting in a decrease of petitioners' federal tax from \$33,558.00 to \$14,622.00.

Accelerated depreciation		\$ 3,084
Capital gains, section 1202 deduction	\$560,415	
Less: NOL carryforward	(197,674)	
NOL carryback, 1973	<u>(189,609)</u>	
Net section 1202 capital gains		<u>173,132</u>
Revised total tax preference income		<u>176,216</u>
Tax computed due		<u><u>\$ 14,622</u></u>

3. On December 20, 1976, petitioners filed with the Service a refund claim, seeking to carry back to the 1972 year a net operating loss of \$77,956.00 incurred in 1975. This loss was applied against the 1972 tax preference income, reducing petitioners' revised federal tax of \$14,622.00 to \$6,836.00.

Accelerated depreciation		\$ 3,094
Capital gains, section 1202 deduction	\$560,415	
Less: NOL carryforward	(197,674)	
NOL carryback, 1973	(189,609)	
NOL carryback, 1975	<u>(77,956)</u>	
Net section 1202 capital gains		<u>95,176</u>
Revised total tax preference income		<u>98,260</u>
Revised tax due		<u><u>\$ 6,836</u></u>

4. On April 26, 1977, the Service concluded its examination of petitioners' 1972 return and accepted the return, including the net operating **loss** carry-forwards and carrybacks, as filed. Petitioners' revised federal tax liability,

Original tax computed per 1972 return		\$33,558
Less: 1973 NOL carryback refund	18,961	
1975 NOL carryback refund	7,796	
		<u>(26,757)</u>
Revised liability		\$ 6,801

The federal adjustments were based on proposed regulation section 1.57-4.

5. On their 1972 New York State resident return, petitioners reported adjusted gross income of \$39,623.00 and items of tax preference of \$365,825.00, which they modified as shown in the following computations:

(a) Personal income tax

Federal adjusted gross income	\$ 39,623
Add: capital gain modification, section 612(b)(11)	
20% x \$560,412	112,083
Less: interest income on U.S. obligations	<u>(4,983)</u>
Total N.Y. income	\$146,722
Less: itemized deductions	(16,783)
exemptions	<u>(3,900)</u>
N.Y. taxable income	\$126,039
Personal income tax	\$ 17,216

(b) Minimum income tax

Federal items of tax preference	\$365,825
Less: capital gain modification, section 622(b)(4)	
20% x \$560,412	(112,083)
specific deduction	(5,000)
personal income tax	<u>(17,216)</u>
Minimum taxable income	\$231,526
Minimum tax	\$ 13,892

(c) Total tax liability

Personal income tax	\$ 17,216
Minimum tax	13,892
Surcharge	778
Total	<u>\$ 31,886</u>

6. On or about November 12, 1975, petitioners submitted to the Audit Division a claim for refund of \$13,426.00 for the taxable year 1972, based on the carryback of the 1973 net operating loss of \$189,609.00. According to

petitioners' calculation, the carryback reduced their minimum taxable income to \$43,748.00.

Accelerated depreciation	\$ 3,084
Capital gains, I.R.C. section 1202 deduction	560,415
Less: NOL carryforwards	(197,674)
NOL carryback, 1973	(189,609)
	<u>\$176,216</u>
Less: capital gain modification, section 622(b)(4)	(112,083)
specific deduction	(5,000)
personal income tax (also reduced)	(15,385)
Minimum taxable income	<u>\$ 43,748</u>
Minimum tax	\$ 2,625

7. By notice dated December 20, 1976, the Audit Division advised petitioners that their refund claim of \$13,426.00 was partially disallowed in the amount of \$5,769.00. The Division calculated the modification to the item of tax preference for capital gains by applying 20 percent to the capital gains deduction as reduced by the net operating **loss** carryforwards and carryback.

Capital gains deduction	\$560,415
Less: NOL carryforwards, 1970 and 1971	(197,674)
NOL carryback, 1973	(189,609)
Capital gains deduction remaining	<u>\$173,132</u>
Less: capital gain modification	(34,626)
Capital gains deduction	<u>\$138,506</u>
Accelerated depreciation	<u>3,084</u>
Items of tax preference	<u>\$141,590</u>

Petitioners, on the other hand, had applied the 20 percent modification to the full deduction.

8. On or about October 15, 1976, petitioners submitted a refund claim, together with an amended personal income tax return, requesting a refund in the amount of \$24,745.00, premised on the carryback to 1972 of a net operating **loss** incurred in 1975. Their revised computations of their 1972 personal income tax and minimum income tax liability are set forth below.

(a) Minimum income tax

Accelerated depreciation		\$ 3,084
Capital gains, I.R.C. section 1202 deduction	560,415	
Less: NOL carryforward	(197,674)	
NOL carryback, 1973	(189,609)	
NOL carryback, 1975	(77,956)	
Capital gains deduction remaining		<u>95,176</u>
Items of tax preference		<u>\$98,260</u>
Less: capital gains modification		
20% x \$95,176		<u>(19,035)</u>
Total items of tax preference		<u>\$79,035</u>
Minimum tax, after specific deduction and personal income tax		\$ 4,274

(b) Personal income tax

Federal adjusted gross income	\$39,623
Add: capital gains modification	
20% x \$95,176	19,035
Less: interest income on U.S. obligations	<u>(4,984)</u>
Total N.Y. income	<u>\$53,674</u>
Personal income tax, after itemized deductions and exemptions	\$ 2,997

(c) Total tax liability

Personal income tax	\$ 2,997
Minimum tax	4,274
Surcharge	<u>182</u>
Tax due	<u>\$ 7,453</u>
Tax withheld	<u>(312)</u>
Net tax due	<u>\$ 7,141</u>
Less: tax originally computed	<u>(31,886)</u>
Tax overpayment	<u>\$24,745*</u>

* The \$24,745.00 overpayment was computed, not giving effect to the amount of \$7,657.00 previously refunded.

The Audit Division has no record of having received petitioners' October 15, 1976 refund claim.

CONCLUSIONS OF LAW

A. That the minimum taxable income of resident individuals is calculated in accordance with Tax Law section 622. Subsection (b), paragraph (4) of such

"The federal item of tax preference for capital gains shall be computed by subtracting from such tax preference item one-fifth of the net long-term capital gain deduction,"

The federal item of tax preference for capital gains must be reduced by available net operating **loss** carrybacks and carryforwards before computation of the modification required by section 622(b)(4). This treatment **is in** consonance with the computation of the addition modification to federal adjusted gross income required by section 612(b)(11) in arriving at New York adjusted gross income: the net capital gain deduction of Internal Revenue Code section 1202 is similarly reduced by loss carrybacks and carryforwards. Indeed, petitioners effectively conceded these principles by their assertion that their 1972 tax liability is properly reflected in the refund claim dated October 15, 1976 (Finding of Fact "8").

B. That petitioners are entitled to a refund or credit in the amount of \$24,745.00, less any amount previously credited or refunded to them. They submitted their claim to the Audit Division in a timely fashion and satisfactorily proved the 1975 net operating loss by, inter alia, documentary evidence of allowance of the same loss by the Internal Revenue Service.

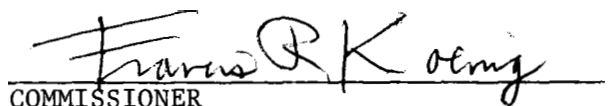
C. That the petition of James H. and Emily M. Scheuer is granted to the extent indicated in Conclusion of Law "B", and the Audit Division is directed to process their claim for credit or refund in accordance therewith.

DATED: Albany, New York

STATE TAX COMMISSION

JAN 17 1986


PRESIDENT


COMMISSIONER

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