

STATE OF NEW YORK  
STATE TAX COMMISSION

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In the Matter of the Petition  
of  
MUTUAL BROADCASTING SYSTEM INC. : DECISION  
for Redetermination of a Deficiency or for  
Refund of Corporation Franchise Tax under  
Article 9-A of the Tax Law for the Years 1973  
and 1979.

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Petitioner, Mutual Broadcasting System, Inc., 7575 East Fulton Road, Ada, Michigan 49355, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the years 1978 and 1979 (File No. 58244).

A hearing was held before Arthur Johnson, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on January 14, 1987 at 9:15 A.M., with all briefs to be submitted by May 27, 1987. Petitioner appeared by Thomas Zandstra. The Audit Division appeared by John P. Dugan, Esq. (Gary Palmer, Esq., of counsel).

ISSUES

- I. Whether petitioner is entitled to a net operating loss carryback.
- II Whether a penalty imposed for late filing of Federal tax changes should be cancelled.

FINDINGS OF FACT

1. Mutual Broadcasting System, Inc. was a national network radio broadcaster, which operated as a subsidiary of Mutual Broadcasting Corporation prior to September 30, 1977.

2. On September 30, 1977, Amway Communications Corporation ("Amway I") purchased all the assets of Mutual Broadcasting Corporation which consisted of the following:

100% of the stock of Mutual Broadcasting System, Inc.  
100% of the stock of Mutual Sports, Inc.  
51% of the stock of Mutual Reports, Inc.

The corporations operated under the above structure from September 30, 1977 through May 30, 1978.

3. On May 31, 1978, Mutual Broadcasting System, Inc., Mutual Sports, Inc. and Mutual Reports, Inc. were liquidated into Amway I in a tax free liquidation under Internal Revenue Code § 334(b)(2).

4. The name of Amway I was then changed to Mutual Broadcasting System, Inc. Accordingly, said corporation is the petitioner herein.

5. Also on May 31, 1978, Amway Communications Corp. ("Amway II") was formed to hold the stock of Amway I.

6. For the fiscal year ending August 31, 1978, a combined New York State Franchise Tax Report was filed which included the following entities:

<u>Corporation</u>	<u>Period</u>
Amway II	5/13/78-8/31/78
Mutual Broadcasting System, Inc.	9/30/77-5/30/78
Mutual Broadcasting System, Inc. (formerly Amway I)	9/30/77-8/31/78
Mutual Sports, Inc.	9/30/77-5/30/78

7. For the period ending August 31, 1980, petitioner sustained a net operating loss. Petitioner filed a consolidated Federal return with other affiliated corporations. The Federal net operating loss on a separate basis for petitioner for the fiscal year ending August 31, 1980 was \$5,113,421.00. The corresponding New York State net operating loss for petitioner for the same period was adjusted to \$4,650,198.00, which represented the Federal loss

reduced by the addback of interest expense deemed to be indirectly attributed to subsidiary capital pursuant to Tax Law § 208.9(b)(6)

8. On May 11, 1984, petitioner filed a report of change in taxable income by the United States Treasury Department, which increased petitioner's income for 1978 by \$1,045,675.00.

9. On May 11, 1984, petitioner also filed a claim for refund based on a carryback of the August 31, 1980 net operating **loss** to the fiscal years ending August 31, 1978 and August 31, 1979.

10. The Audit Division disallowed the entire net operating loss deduction of \$4,950,660.00 for the fiscal year ending August 31, 1978 while allowing \$1,404,851.00 of the net operating loss as a carryback to the fiscal year ending August 31, 1979.

11. On November 15, 1984, the Audit Division issued a Statement of Audit Adjustment to petitioner for the fiscal year ending August 31, 1978, increasing petitioner's Federal taxable income by \$1,045,675.00, based on the Federal adjustment, disallowing the net operating **loss** and asserting that an additional tax of \$21,390.00 was due. In disallowing the net operating **loss** deduction, the statement explained:

"The \$4,950,660.00 net operating **loss** deduction claimed as a carryback from your 8/80 **loss** period of Mutual Broadcasting (successor corp.) to the combined group's 8/73 taxable period, has been disallowed.

**For** the periods involved, section 381 of the Internal Revenue Code allowed net operating **loss** carryovers to the surviving (acquiring) corporation in certain tax-free mergers or reorganizations (unless Section 334(b) (2) applied). Only the survivor of a Section 368(a)(1)(F) reorganization was allowed to carryback losses against pre-merger income. A merger under Section 334(b)(2) -- as in your instance -- was (and is still) precluded from carrying over and/or carrying back any pre/post-merger losses.

**With respect to the net operating loss you incurred for the period ended 8/80. it is allowed only to the extent that it can be carried**

Based **on** the aforementioned, the first taxable period (**of** your own taxable entity) to which your 8/80 loss may be applied **is** the period ended 8/79.

Since you did not report the increase **in** federal taxable income (based on the adjustments made by the U.S. Treasury Department) within 90 days of determination, penalty has been imposed for late filing of the federal change."

12. Also on November 15, 1984, the Audit Division issued a Notice of Deficiency to petitioner for \$21,390.00 **in** tax, interest of \$16,824.20 and an "additional charge" (penalty) of \$5,347.00 for the fiscal year ending August 31, 1978, less credits of \$7,071.16 for the fiscal year ending August 31, 1979 and \$16,020.83 for the fiscal year ending August 31, 1980.

#### CONCLUSIONS OF LAW

A. That, as a general rule, the deduction of a net operating **loss** carryback or carryover **is** personal to the taxpayer who sustained the loss (New Colonial Ice Co. v. Helvering, 292 US 435) .

B. That exceptions to the aforesaid general rule may be found in Internal Revenue Code § 381(a), which deals with carryovers **in** certain corporate liquidations and reorganizations.

C. That since the transaction at issue involved a liquidation under Internal Revenue Code § 334(b)(2), the carryover provisions of Internal Revenue Code § 381(a) are inapplicable (see Internal Revenue Code § 381[a][1]). Accordingly, the loss may be deducted only by petitioner.

D. That petitioner's reliance on Treas. Reg. § 1.1502 et seq., dealing with consolidated Federal tax returns, **is** misplaced. As petitioner, the corporation which sustained the **loss**, was a member of a combined group during the income year, the loss may be deducted only as provided in 20 NYCRR 3-8.7(a). Petitioner has not shown that it is entitled to an additional deduction under

E. That petitioner did not sustain **its** burden of proof under Tax Law § 1089(e) **to show** reasonable cause; accordingly, the penalty asserted must stand (20 NYCRR 9-1.5).

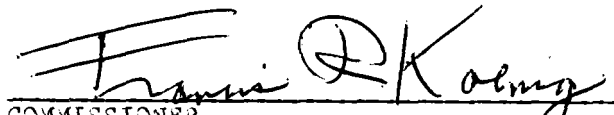
F. That the petition of Mutual Broadcasting System, Inc. **is** denied and the Notice of Deficiency issued November 15, 1984, is sustained.

DATED: Albany, New York

STATE TAX COMMISSION

AUG 27 1981

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER