STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

THEODORE S. and GEORGINE Θ. PROKOPOV DECISION

for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Years 1981 and 1982.

Petitioners, Theodore S. and Georgine Θ. Prokopov, Box 72, Lake Guymard, Godeffroy, New York 12739, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the years 1981 and 1982 (File No. 59876).

A hearing was held before Robert F. Mulligan, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York on March 4, 1986 at 1:15 P.M. Petitioners appeared pro se. The Audit Division appeared by John P. Dugan, Esq. (Angelo A. Scopellito, Esq., of counsel).

ISSUES

I. Whether petitioners are entitled to investment tax credits for residential real property built to be sold at a profit.

II. Whether section 683(c)(5) of the Tax Law, which provides that recovery of an erroneous refund may be made within two years from the making of the refund, supersedes the provision for assessment within three years in section 683(a) of the Tax Law.

FINDINGS OF FACT

1. Petitioners, Theodore S. and Georgine Θ. Prokopov, filed separately on one New York State Resident Income Tax Return for the year 1981. They claimed the following investment tax credits: husband, $641.60; wife, $1,282.28. The

property on which credit was claimed was described as a two story colonial house acquired in 1980 with the principal use "(r)esidential rental property to be sold for profit". Refund of $1,730.32 was requested and a refund of $1,486.04 was allowed and issued on June 10, 1982. (The difference was apparently attributable to withholding and/or estimated tax variances.)

2. Petitioners filed a joint New York State income tax return for 1982 on which they claimed an investment tax credit of $600.70. The property description and principal use were similar to those set forth on the 1981 return, except it was indicated that the house was built in 1979. Refund of $1,233.60 was requested and allowed. The date of issuance of the refund does not appear in the record. Petitioners' return was undated; the only assumption that can be made is that it was filed by April 15, 1983, since there was no indication that it was untimely. Accordingly, the refund would have been required to have been issued by July 15, 1983.

3. On January 24, 1985, the Audit Division sent a statement of audit changes to petitioners disallowing the claimed investment tax credits with the following explanation:

> "The property reported on Form IT-212, or the depreciation schedule attached to your return is not considered qualified for the New York State investment tax credit as it is not principally used in the production of goods by manufacturing, processing, assembling, refining, mining, extracting, farming, agriculture, horticulture, floriculture, viticulture or commercial fishing."

4. On April 5, 1985, the Audit Division issued notices of deficiency to petitioners as follows:

NAME	YEAR	ADDITIONAL TAX DUE
Theodore S. & Georgine O. Prokopov	1981	$ 641.60
Georgine O. Prokopov	1981	1,282.28
Theodore S. & Georgine O. Prokopov	1982	600.00

The notices of deficiency also computed interest due on the deficiencies.

5. The houses were built by petitioners for resale at a profit. Petitioner were not able to sell them until after the years at issue. During the years at issue, the houses were rented and rental income was received.

6. Petitioners argue that the disallowance of the investment tax credit for construction of real property used for rental purposes or for resale at a profit is discriminatory. They also argue, in the alternative, that the notices of deficiency were not timely, since the two year limitation on assessmen provided for in section 683(c)(5) of the Tax Law supersedes the three year limitation on assessment set forth in section 683(a) of the Tax Law, with respect to erroneous refunds.

CONCLUSIONS OF LAW

A. That section 606(a) of the Tax Law provides an investment credit against personal income tax. Paragraph (2) of subsection (a) provides, in pertinent part, as follows:

> "(2) A credit shall be allowed under this subsection with respect to tangible personal property and other tangible property, including buildings and structural components of buildings, which are: depreciable pursuant to section one hundred sixty-seven of the internal revenue code or recovery property with respect to which a deduction is allowable under section 168 of the internal revenue code,[3] have a useful life of four years or more, are acquired by purchase as defined in section one hundred seventy-nine (d) of the internal revenue code, have a situs in this state and are principally used by the taxpayer in the production of goods by manufacturing, processing, assembling, refining, mining, extracting, farming, agriculture, horticulture, floriculture, viticulture or commercial fishing..." (emphasis supplied).

(See also: 20 NYCRR 103.1(c) and (d). This regulation was effective January 28, 1982.)

B. That the buildings constructed by petitioners were not principally used by the petitioners in production of goods by manufacturing, processing or any of the other means specified in the statute. Accordingly, the investment credits are not allowable.

C. That the State Tax Commission has no jurisdiction to determine if a statute is unconstitutionally discriminatory.

D. That section 683 of the Tax Law provides, in pertinent part, as follows:

> "Section 683. Limitations on Assessment
>
> (a) General. - Except as otherwise provided in this section, any tax under this article shall be assessed within three years after the return was filed (whether or not such return was filed on or after the date prescribed).
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> * * *
>
> (c) Exceptions. -
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> * * *
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> (5) Recovery of erroneous refund. - An erroneous refund shall be considered an underpayment of tax on the date made, and an assessment of a deficiency arising out of an erroneous refund may be made at any time within two years from the making of the refund, except that the assessment may be made within five years from the making of the refund if it appears that any part of the refund was induced by fraud or misrepresentation of a material fact."

E. That while the term "erroneous refund" is not defined in the Tax Law, examination of comparable sections of the Internal Revenue Code is useful in analyzing the New York statute. Section 6501(a) of the Internal Revenue Code provides as follows:

> "(a) GENERAL RULE. - Except as otherwise provided in this section, the amount of any tax imposed by this title shall be assessed within 3 years after the return was filed (whether or not such return was filed on or after the date prescribed) or, if the tax is payable by stamp, at any time after such tax became due and before the expiration of 3 years after the date on which any part of such tax was paid, and no proceeding in court without assessment for the collection of such tax shall be begun after the expiration of such period."

Erroneous refunds are not listed as an exception under section 6501(c) but are treated separately. Section 7405 of the Internal Revenue Code provides that refunds of taxes erroneously made after the expiration of a period of limitation or which are otherwise erroneous, may be recovered by civil action brought in the name of the United States. Section 6532(b) of the Internal Revenue Code provides as follows:

> "(b) **SUITS** BY UNITED STATES FOR RECOVERY OF ERRONEOUS REFUND. - Recovery of an erroneous refund by suit under section 7405 shall be allowed only if such suit is begun within 2 years after the making of such refund, except that such suit may be brought at any time within 5 years from the making of the refund if it appears that any part of the refund was induced by fraud or misrepresentation of a material fact."

Expiration of the two year limitation for suit to recover an erroneous refund (Section 6532[b]) does not bar assessment under the three year limitation (Section 6501[a]). Warner v. Commissioner, 526 F.2d 1 (9th Cir. 1975). In Warner, the Ninth Circuit Court of Appeals also rejected the taxpayers' claim of estoppel:

> "The appellants also invoke a form of 'estoppel' that rests on the notion that the Commissioner ought not to make refunds and reserve the right to get them back when an ordinary examination of the return would have indicated that the full amount of the refund was not allowable. Alas, the Commissioner, confronted by millions of returns and an economy which repeatedly must be nourished by quick refunds, must first pay and then look. This necessity cannot serve as a basis of 'estoppel'." (Id. at 2.)

F. That recognizing that the Federal and State statutes are dissimilar to the extent that the Federal erroneous refund recovery provision requires a civil suit rather than an assessment, the principles behind each procedure are the same and the rationale in Warner may be applied here. Expiration of the two year period in section 685(c)(5) of the Tax **Law** does not bar assessment under section 683(a). It is particularly noted that section 683(c)(5) provides that assessment "may" be made at any time within two years from the date of the refund or five years in the event of fraud or misrepresentation. The language is permissive, not mandatory. Accordingly, the three year period of limitation applies.

G. That since there was no showing that the refunds were induced by fraud or misrepresentations of a material fact, no interest *is* due on the deficiencies. Section 684(m) of the Tax Law.

H. That except for cancellation of interest, the petition of Theodore S. and Georgine O. Prokopov is denied and the notices of deficiency are otherwise sustained.

DATED: Albany, New York

OCT 07 1986

STATE TAX **COMMISSION**

PRESIDENT

COMMISSIONER

COMMISSIONER