

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
SAM AND MIRIAM GOLDSTEIN : DETERMINATION
 : DTA NO. 829245
for Redetermination of Deficiency or for Refund of :
New York State and New York City Personal Income Tax :
under Article 22 of the Tax Law and the New York City :
Administrative Code for the Year 2014. :

Petitioners, Sam and Miriam Goldstein, filed a petition for redetermination of deficiency or for refund of New York State personal income tax under article 22 of the Tax Law and the New York City Administrative Code for the year 2014.

The Division of Taxation, by its representative, Amanda Hiller, Esq. (Christopher O'Brien, Esq., of counsel), brought a motion, dated October 2, 2020, seeking an order granting summary determination in the above-referenced matter pursuant to section 3000.9 (b) of the Rules of Practice and Procedure of the Tax Appeals Tribunal. Petitioners, appearing by Barclay Damon LLP (David G. Burch, Jr., Esq., of counsel) filed a response dated October 30, 2020. The 90-day period for issuance of this determination commenced on November 1, 2020. Based upon the motion papers, the affidavits and documents submitted therewith, and all pleadings and documents submitted in connection with this matter, Nicholas A. Behuniak, Administrative Law Judge, renders the following determination.

ISSUE

Whether the Division of Taxation's motion for summary determination should be granted.

FINDINGS OF FACT

1. B&H Foto & Electronics Corp. (B&H Foto) is a New York corporation located in New York City.
2. B&H Foto is taxed under Subchapter S of the Internal Revenue Code.
3. B&H Foto was certified in the North Brooklyn/Brooklyn Navy Yard/East Williamsburg Empire Zone as a qualified empire zone enterprise (QEZE) with an effective date of March 7, 2002.
4. The corporate tax returns filed for B&H Foto for the 2014 tax year included form 1120S (US income tax return for an S corporation), form CT-3-S (New York S corporation franchise tax return), and NYC 3L (New York City general corporation tax return). Petitioners assert that B&H Foto did not file income tax returns with any other state.
5. B&H Foto's relevant CT-3-S included form CT-604 (claim for QEZE tax reduction credit).
6. Petitioners directly and through multiple trusts own 50% of the stock of B&H Foto.
7. Petitioners have represented that all of B&H Foto's employees and assets are situated within the state of New York.
8. Petitioners filed a joint IT-201 (NYS resident income tax return) for the 2014 tax year and claimed the QEZE tax reduction credit as shareholders of B&H Foto's certification as a QEZE. Petitioners' tax factor was computed on their form IT-604 (claim for QEZE tax reduction credit) which was filed with their IT-201.
9. The calculation of petitioners' benefit period, employment increase and zone allocation factors utilized in their 2014 tax return for calculation of their relevant QEZE tax reduction credit were not challenged by the Division of Taxation (Division).

10. Petitioners calculated their tax factor component of the QEZE tax reduction credit without utilization of the B&H Foto's business allocation percentage (BAP).

11. The BAP of B&H Foto for the 2014 tax year as reported on its 2014 CT-3-S-ATT (attachment to form CT-3-S) was 17.74%.

12. On audit, the Division applied the BAP of B&H Foto as a component of petitioners' tax factor calculation, and reduced petitioners' QEZE tax reduction credit claimed from \$291,819.00 to \$51,768.00.

13. The Division sent petitioners a letter, dated March 6, 2017, informing petitioners that their QEZE tax reduction credit had been reduced. The Division sent petitioners an account adjustment notice, dated April 13, 2017, informing petitioners that their refund sought was reduced from \$1,171,690.00 to \$931,639.00.

14. On March 6, 2019, petitioners filed a petition seeking a refund relating to the Division's reduction of petitioners' QEZE tax reduction credit.

15. On June 5, 2019 the Division filed an answer in response to the petition.

16. The Division filed a motion, dated October 2, 2020, seeking an order granting summary determination in the above-referenced matter pursuant to section 3000.9 (b) of the Rules of Practice and Procedure of the Tax Appeals Tribunal (Rules). Included with the motion was the affirmation of Christopher O'Brien, Esq., and the affidavit of the Division's Tax Technician IV, Fredrick Houser.

17. Petitioners filed a response, dated October 30, 2020, to the Division's motion, asserting that the Division's adjustments to petitioners' tax factor was inappropriate and thus summary determination was unwarranted. Included with the response was the affirmation of David G. Burch, Jr., Esq.

CONCLUSIONS OF LAW

A. A motion for summary determination shall be granted:

“if, upon all papers and proof submitted, the administrative law judge finds that it has been established sufficiently that no material and triable issue of fact is presented and that the administrative law judge can, therefore, as a matter of law, issue a determination in favor of any party” (20 NYCRR 3000.9 [b] [1]).

B. Tax credits are considered a “particularized species of exemption from tax” (*Matter of Taxel*, Tax Appeals Tribunal, July 9, 2020, citing *Matter of Grace v New York State Tax Commn.*, 37 NY2d 193 [1975], *rearg denied* 37 NY2d 816 [1975], *lv denied* 338 NE2d 330 [1975]), and taxpayers bear the burden of establishing their entitlement thereto (*Matter of Golub Serv. Sta. v Tax Appeals Trib. of State of N.Y.*, 181 AD2d 216, 219 [3d Dept 1992]). Petitioners must establish that their interpretation of the statute is the only reasonable interpretation (*Matter of Hucko Trust*, Tax Appeals Tribunal, September 19, 2013).

C. This proceeding concerns petitioners’ entitlement to a QEZE tax reduction credit that they claimed for tax year 2014 as pass-throughs from B&H Foto, a New York corporation. B&H Foto was certified as a QEZE effective March 7, 2002. B&H Foto is an S corporation, which is a “flow-through” or “pass-through” entity for purposes of taxation. As such, its income and any applicable QEZE tax reduction credits pass through to its shareholders, including the petitioners who are New York residents, and are reported on the personal income tax returns that petitioners file.

D. During the relevant tax year, petitioners claimed a QEZE tax reduction credit on their personal income tax return. The amount of a QEZE tax reduction credit is the product of four factors: the benefit period factor, the employment increase factor, the zone allocation factor and the tax factor (*see* Tax Law § 16 [b]-[f]). The first three factors are decimal numbers with values

between 0.0 and 1.0, and the tax factor is a dollar amount based upon the tax imposed by New York law on the taxpayer that is attributable to the QEZE's income. The Division does not challenge petitioners' 2014 benefit period factor, employment increase factor or zone allocation factor. For a shareholder of a New York S corporation that is a QEZE, the tax factor is the portion of the shareholder' total New York income tax equal to "the ratio of the shareholder's income from the S corporation *allocated within the state*, entering into New York adjusted gross income, to the shareholder's New York adjusted gross income" (Tax Law § 16 [f] [2] [C] [emphasis added]).

E. Upon review of petitioners' personal income tax return for 2014, the Division determined that petitioners miscalculated their QEZE tax reduction credit by failing to exclude the state income taxes that were attributable to B&H Foto's out-of-state income when calculating the tax factor, because such income was not "allocated within the state" as required by Tax Law § 16 (f) (2) (C). To determine the portion of B&H Foto' income that was allocated within the state, the Division utilized B&H Foto's BAP as reported on B&H Foto's own 2014 form CT-3-S-ATT. On B&H Foto's 2014 form CT-3-S-ATT, it reported a BAP of 17.74%. Based on application of B&H Foto's BAP to petitioners' tax factor, the Division reduced the petitioners' refund demand from \$1,171,690.00 to \$931,639.00.

F. Petitioners challenged the Division's determination, arguing that the Division erred by applying B&H Foto' BAP to determine the amount of B&H Foto' income that was allocated within the state when it calculated petitioners' tax factor.

G. The tax factor for a shareholder of a New York S corporation that is a QEZE is the portion of his or her New York income tax that is attributable to the income of the S corporation (*see* Tax Law § 16 [f] [2] [C]).

“Such attribution shall be made in accordance with the ratio of the shareholder’s income from the S corporation *allocated within the state*, entering into New York adjusted gross income, to the shareholder’s New York adjusted gross income, or in accordance with such other methods as [respondent Commissioner of Taxation and Finance] may prescribe as providing an apportionment which reasonably reflects the portion of the shareholder’s tax attributable to the income of the qualified empire zone enterprise. In no event may the ratio so determined exceed 1.0” (Tax Law § 16 [f] [2] [C] [emphasis added]).

In this regard, the Appellate Division has held:

“Allocation of a New York S corporation’s income within the state to a nonresident shareholder’s New York adjusted gross income is determined by application of the BAP reported by the corporation. When calculating QEZE credits, it is rational to interpret Tax Law § 16 (f) to require similar allocation of a New York S corporation’s income for resident shareholders based on the BAP reported by the corporation” (*see Matter of Purcell v New York State Tax Appeals Trib.*, 167 AD3d 1101 [3d Dept 2018], *appeal dismissed* 33 NY3d 999 [2019], *lv denied* 33 NY3d 913 [2019]).

H. Petitioners’ main argument is that the court’s holding in *Purcell* does not apply to the current case at hand because in *Purcell*, the S corporation at issue had operations in both New York and Virginia, whereas in the case at hand, the S corporation at issue has all of its operations within New York State and not in any other state. Petitioners are correct that the court in *Purcell*, in providing a summary of the facts, does note that the S corporation at issue in that case had operations both within and outside of New York State; however, the court in *Purcell* did not limit the required application of an S corporation’s BAP to a shareholder’s tax factor to such limited circumstances. Rather, as noted in the above quote from *Purcell*, the court made the broad statement that the adjustment applies to “resident shareholders” and provided no limitations as sought by petitioners. With regard to petitioners’ claim in this case, the court in *Purcell* appeared to find that the Tax Law already addresses this concern when it noted:

“QEZE tax reduction credits are not available based on all business activity conducted by a QEZE in New York. Rather, the zone allocation factor restricts

the availability of such credits to activity that occurs only within an empire zone, as measured by capital investment and employment expense (*see* Tax Law § 16 [e] [1], [2])” (*id.* at footnote 3).

I. Even if petitioners’ claim that B&H Foto’s operations were only in New York State was accurate, the Division has met its burden establishing that summary determination is warranted in this case since that fact would not change the outcome of this case. Petitioners have failed to establish that their interpretation of the applicable Tax Law is the only reasonable interpretation. There are no material facts at issue that change the conclusions found herein.

J. Petitioners also argue that the approach advanced by the Division is not consistent with the relevant tax forms for the subject credit at issue. However, tax forms and instructions are accorded limited weight and thus are not controlling so this argument fails especially in light of the case law on point (*see* 20 NYCRR 2375.8 [c]).

K. Accordingly, the Division’s motion for summary determination is granted, the petition of Sam and Miriam Goldstein is denied, and the account adjustment notice of April 13, 2017 is sustained.

DATED: Albany, New York
January 28, 2021

/s/Nicholas A. Behuniak
ADMINISTRATIVE LAW JUDGE