STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
SCHENECTADY TURBINE SERVICES, LTD.	:	DECISION DTA No. 809757
for Redetermination of a Deficiency or for Refund of Corporation Franchise tax under Article 9-A of the Tax Law for the Fiscal Year ended January 31, 1978.	:	

Petitioner Schenectady Turbine Services, Ltd., R.D. #2, Route 50, Ballston Spa, New York 12020, filed an exception to the determination of the Administrative Law Judge issued on March 25, 1993. Petitioner appeared by Ertel, Kristel and Sicilia, P.C. (Daniel Ertel, C.P.A.) The Division of Taxation appeared by William F. Collins, Esq. (Robert J. Jarvis, Esq., of counsel).

Both petitioner and the Division of Taxation submitted briefs. Petitioner submitted a reply brief. Oral argument, requested by petitioner, was heard on September 13, 1993 and began the six-month time period for the issuance of this decision.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUES

I. Whether the Division of Taxation agreed to waive penalties imposed against petitioner for the fiscal year ended January 31, 1978 in exchange for petitioner's payment of interest due on its late payment of tax due for such year.

II. Assuming no such agreement existed, whether petitioner is entitled to a refund of its interest payment and the issuance of a Notice of Deficiency for interest and penalties, which would allow petitioner to challenge both the interest and penalty portions of such a deficiency.

III. Whether petitioner has established sufficient basis to warrant abatement of the penalties.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Petitioner, Schenectady Turbine Services, Ltd., is a wholly-owned subsidiary of Charlton Industries, Inc. ("Charlton"). Petitioner is engaged in the business of selling new and used turbine parts.

On or about April 17, 1984, following an Internal Revenue Service ("IRS") audit examination, Charlton received an IRS examination report reflecting and explaining proposed deficiencies in tax for each of its fiscal years ended January 31, 1977 through January 31, 1981, inclusive. Charlton apparently disagreed with the results of the audit examination for at least some of the years audited, as reflected by the IRS's June 30, 1985 issuance of a Notice of Deficiency to Charlton asserting additional tax due for the fiscal years ended January 31, 1977, 1979, 1980 and 1981.[1] In turn, this asserted deficiency was resolved on December 29, 1986, via a Tax Court approved negotiated settlement between the IRS and Charlton.

Upon receiving information from the IRS that Charlton's Federal taxable income had been changed for the FYE 1977 through 1981, the Division of Taxation ("Division") issued a letter to Charlton on June 10, 1987, requesting that such Federal changes be reported to New York State on the requisite Form CT-3360 ("Report of Change of Federal Taxable Income"). When no response was received, a second, similar letter, dated January 8, 1988, was also sent to petitioner. Again, there was no response from either Charlton or from petitioner.

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[1]The term "fiscal year (or years) ended" is sometimes abbreviated hereinafter as "FYE."

Since no response had been received with regard to either of the above letters, an assessment was issued against Charlton on March 17, 1988, seeking corporation franchise tax due, as based on the Federal changes, from Charlton.[2]

Thereafter, on or about December 21, 1989, Forms CT-3360 for the FYE January 31, 1977 through January 31, 1980 were filed with the Division on behalf of petitioner, Schenectady Turbine Services, Ltd. These forms were accompanied by full payment of the tax computed as due thereon, together with a letter dated December 21, 1989 advising the Division that its assessment against Charlton should properly be imposed against petitioner. Petitioner's Form CT-3360 filed for the FYE January 31, 1978 reflects tax due to New York State (based on the Federal changes) in the amount of $106,963.00.[3] This form lists, on its face, May 28, 1985 as the "date of notice of final Federal determination." A copy of the final Federal adjustments for the FYE January 31, 1978 was not attached to Form CT-3360 as offered in evidence.

Since the Federal changes had not been reported to New York State within 90 days of final Federal determination, the Division determined that penalties for late filing and negligence, and interest based on late payment of tax, were owed. In turn, a Statement of Audit Adjustment dated July 9, 1990 was issued to petitioner, reflecting for the FYE January 31, 1978 interest due in the amount of $219,783.71, plus penalties due in the aggregate amount of $30,989.00. The amounts of interest and penalties shown represent amounts calculated after allowing petitioner credit for the $106,963.00 tax amount paid with Form CT-3360, as well as other adjustments not relevant here. The Statement of Audit Adjustment also specified that the penalties in question were those provided for under Tax Law § 1085(a) and (b) (late filing and negligence).

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[2]A copy of the "assessment" issued to Charlton is not included in the record. However, correspondence offered in evidence by both parties clearly references the issuance of an "assessment" against Charlton on March 17, 1988 (see, Exhibits "H," "6").

[3]It is noted that the FYE January 31, 1978 was not included on the June 30, 1985 IRS Notice of Deficiency. However, the IRS examination report in evidence shows a disallowed partnership loss for Charlton's FYE January 31, 1978, as well as a tax deficiency of $1,181,971.00 for such year (see, Exhibit "7").

On July 19, 1990, a Notice of Deficiency was issued to petitioner. This notice pertained to petitioner's FYE January 31, 1978 and asserted penalties due in the amount of $309.89 plus interest due in the amount of $2,204.46.

The Division alleges that the July 19, 1990 Notice of Deficiency, described above, corresponds to the July 9, 1990 Statement of Audit Adjustment, also described above, noting that these documents bear matching assessment numbers (C900709130N). However, the Division maintains that the July 19, 1990 Notice of Deficiency is facially incorrect as the result of a key punching error. More specifically, the Division alleges that the last two digits of the actual amounts due as shown on the July 9, 1990 Statement of Audit Adjustment were accidentally eliminated, with the decimal point moving two places to the left thereby resulting in the July 19, 1990 Notice of Deficiency reflecting much lower amounts than were in fact due.[4] The Division's apparent error was corrected on its accounts receivable system by way of July 20, 1990 adjusting entries to the penalty and interest amounts shown on the Notice of Deficiency, such that the adjusted totals were revised to $30,989.00 for penalty and $219,783.71 for interest (i.e., the accounts receivable system was adjusted to re-enter the amounts as shown on the July 9, 1990 Statement of Audit Adjustment).

On August 29, 1990, petitioner paid in full the aggregate amount of penalty and interest ($2,514.35) shown on the July 19, 1990 Notice of Deficiency.

On or about November 20, 1990, the Division issued to petitioner a Notice and Demand for Payment of the interest and penalty allegedly remaining due, as corrected, in the amount of $259,151.05.[5] Petitioner was also contacted by Division employee Lorraine Alford, and was advised that a balance was still due for the fiscal year in question, consisting of interest in the

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[4]The difference between the interest amounts on the Statement of Audit Changes versus the Notice of Deficiency, according to the Division, represents the increase or accumulation of interest between the July 9, 1990 date of the Statement of Audit Adjustment and the July 19, 1990 date of the Notice of Deficiency, during which time the amount of accumulated interest apparently increased from $219,783.71 to $220,446.00 (such latter figure reflects correction of the decimal point placement).

[5]A copy of this Notice and Demand could not be located by the Division and is, consequently, not included among the documents in evidence. However, there appears to be no dispute between the parties that such Notice was issued to and received by petitioner (see, Exhibit "N"; see also, petitioner's reply brief, p. 4).

amount of approximately $230,000.00, plus penalties of approximately $31,000.00. Ms. Alford was referred to petitioner's representative, Daniel Ertel, C.P.A. According to Mr. Ertel, he suggested that petitioner would pay the interest amount allegedly due if, in return, the Division would agree to waive the penalties. By a letter dated December 21, 1990, Ms. Alford advised Mr. Ertel of the basis upon which penalties were assessed, noting that said penalties "stand as assessed."

On February 6, 1991, Ms. Alford issued a letter to petitioner's representative, Mr. Ertel, responding to his letter of December 26, 1990 (such December 26, 1990 letter is not a part of the record herein). Ms. Alford's letter notes that the Division had no record of receiving any payments or reports (of Federal changes) from petitioner concerning the Federal adjustments prior to petitioner's December 21, 1989 filing of Forms CT-3360. This letter details the bases upon which interest and penalties were imposed. There is no mention in Ms. Alford's February 6, 1991 letter of an agreement to abate penalty based on petitioner's payment of interest amounts.

Included in evidence is a letter dated February 15, 1991 from Mr. Ertel to one Charles Mothon.[6] This letter makes reference to the matter at issue, including statements of the amount of interest and penalty at issue as of the date of the letter. Mr. Ertel's letter also states, in separate paragraphs, that the State had agreed to waive the penalties and that:

> "I believe that payment of the 1/31/79 and 1/31/80 liabilities, excluding the penalties, and getting a receipt for full payment for these years, will formalize the State's agreement to waive the penalties for all years."

On February 27, 1991 petitioner, by its representative, Mr. Ertel, delivered a payment to the Division in the amount of $230,051.66, representing interest alleged to be due for petitioner's FYE January 31, 1978. Accompanying this payment was a letter, dated February 27, 1991, in which petitioner's representative stated:

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[6]Charles Mothon is apparently an officer or employee of either petitioner or its parent, Charlton.

> "The taxpayer waives its right to Notices of Deficiency [for the years 1/31/78 and 1/31/81], and makes full payment thereof, based on the abatement of the assessed penalties" (emphasis added).

By a letter dated April 5, 1991, the Division replied to petitioner's February 27, 1991 letter and payment. The Division's letter describes the foregoing background regarding issuance of a Statement of Audit Adjustment, issuance of a mathematically erroneous Notice of Deficiency, correction thereof via accounts receivable adjusting entries, and issuance of a Notice and Demand for the corrected balance of interest and penalty due. The Division's letter also notes petitioner's payment of the July 19, 1990 Notice of Deficiency, and goes on to provide as follows:

> "[a]s the notice and demand does not avail you of petition rights, we are cancelling the notice and demand and issuing a notice of deficiency for January 31, 1978 for which you will have 90 days to file a petition."

The letter also provides, with regard to the issue of abatement of the penalty, as follows:

> "since the information you recently submitted has not changed the facts as originally presented, we cannot recommend the abatement of penalties that were assessed against Schenectady Turbine Systems [sic], Ltd."

As promised in its April 5, 1991 letter, the Division issued a second Notice of Deficiency to petitioner for the fiscal year ended January 31, 1978. This notice, dated April 19, 1991, asserts penalty due in the amount of $30,989.00 together with accrued interest thereon in the amount of $1,041.00 resulting in an asserted total amount due of $32,030.00. The Division also issued a Statement of Audit Adjustment, dated April 19, 1991, providing information regarding the manner in which the dollar amount asserted as due by the Notice of Deficiency was calculated, as follows:

"Balance Due $32,030.00

Explanation

Deficiency per 3360	$106,963.00
Amount credited from 1/77 3360	3,666.00
Adjusted deficiency	103,297.00
Interest from 4/15/78 to 12/27/89	209,568.00
Penalty (30%)	30,989.00
Total	343,854.00
Amount paid with 3360	106,963.00
Amount paid with 3360 for 1/77	387.00
Deficiency (interest & penalty)	236,504.00
Plus interest to 8/29/90	15,746.00
Total	252,250.00
Less amount paid on 8/29/90	2,514.00
Balance	249,736.00
Interest to 2/27/91	12,331.00
Total	262,067.00
Less amount paid on 2/27/91	230,052.00
Balance	32,015.00
Interest to 4/19/91	15.00
Net deficiency (interest & penalty)	32,030.00

"The above deficiency is based on the CT-3360 filed less any payments made through 2/27/91.

"Penalty is due based on Article 27 of the NYS Tax Law Sections 1085(a) & (b)."

As shown on the above calculations, credit was allowed for the ($230,052.00) interest payment made by petitioner on February 27, 1991, thus leaving only penalty, together with accrued interest thereon, asserted as due per the April 19, 1991 Notice of Deficiency.

By a letter dated May 3, 1991, the Division advised Mr. Ertel of its position that no agreement to waive penalties had been reached with respect to petitioner's case. This letter goes on to advise petitioner's representative that a request for refund (of its interest payment) might be undertaken by the filing of Form CT-8 ("Claim For Credit or Refund").

Petitioner has not paid the balance shown as due on the April 19, 1991 Notice of Deficiency, nor has petitioner filed a claim for refund for any of the payment amounts, including interest, made to date. Petitioner did, however, file a petition contesting the second (April 19, 1991) Notice of Deficiency.

OPINION

In the determination below, the Administrative Law Judge held that because petitioner was late in reporting the Federal change to its taxable income for the fiscal year ended January 31, 1978, the Division was entitled to impose interest and penalties against petitioner (Determination, conclusion of law "C"). The Administrative Law Judge also found that petitioner failed to establish the existence of an agreement between petitioner and the Division whereby petitioner would pay interest due in return for the Division's promise to abate penalties (Determination, conclusion of law "D").

In rejecting petitioner's argument that it would not have paid interest accrued up to the time it filed the report of Federal changes (Form CT-3360) but instead would have awaited a Notice of Deficiency so that it could protest both the interest and penalties, the Administrative Law Judge stated the tax, penalties and interest were assessed at the point the CT-3360 was filed, disposing of petitioner's entitlement to a Notice of Deficiency (Determination, conclusion of law "H"). The Administrative Law Judge found that because petitioner had been afforded full protest rights as to the unpaid penalties without fulfilling any precondition of paying the assessed amounts (as would be required if the Division had simply issued a Notice of Demand), petitioner suffered no detriment from submitting the interest due (Determination, conclusion of law "I"). The Administrative Law Judge also concluded that petitioner failed to establish that interest paid on February 27, 1991 was not due or was in any manner erroneous (Determination, conclusion of law "J"). Finally, the Administrative Law Judge rejected petitioner's contention that penalties imposed should be abated.

On exception, petitioner contends that the Division is precluded from assessing penalties for the late filing of form CT-3360 after accepting petitioner's payment of interest on February 27, 1991, which was made in exchange for the Division's promise to waive penalties. Petitioner also argues that if the Division denies that an agreement existed to abate the penalties, it should

refund the interest voluntarily paid and issue a proper assessment for the interest and the penalty. Finally, petitioner asserts that the penalty should be abated for reasonable cause.

In response, the Division argues that petitioner has not provided any evidence that its failure to comply with the Tax Law was caused by circumstances which warrant abatement of penalties. The Division also argues that it is not required to abate the penalties because of petitioner's payment of interest.

We affirm the determination of the Administrative Law Judge.

Tax Law § 211(3) states that a taxpayer whose taxable income has been changed or corrected by the Internal Revenue Service must report the change or correction to the Division within 90 days after the final determination of such change or correction. The regulation at 20 NYCRR 6-3.1(b) states in part:

> "[a] change in Federal taxable income must be reported on form CT-3360. Form CT-3360 must be accompanied by a copy of the revenue agent's report and copies of all other pertinent information."

At the outset, we note that petitioner does not dispute that section 1085 imposes a penalty for its failure to timely file form CT-3360 reporting the Federal change to its taxable income for the year ended January 31, 1978 (Oral Argument Tr., pp. 6-8; see, Tax Law § 1085[a], [b]). Rather, petitioner argues in the first instance that the Division is precluded from collecting this penalty after accepting petitioner's payment of interest on February 27, 1991, which was made in exchange for the Division's promise to abate the penalties.

The Tax Law specifically authorizes the Division to enter into agreements reducing a taxpayer's liability with respect to taxes (see, e.g., Tax Law §§ 171-eighteenth et seq.). In addition, we have held that where a taxpayer made payments as a condition of an explicit agreement with the Division to abate penalties, the Division may not withdraw its consent to such an agreement after the taxpayer had performed (Matter of Kayton Specialty Shop, Tax

Appeals Tribunal, January 17, 1991). However, we agree with the Administrative Law Judge that:

> "[w]hile petitioner asserts the Division made and then breached such an agreement, the evidence falls short of establishing that such an agreement was in fact made. There is no unequivocal statement in writing evidencing such an agreement, nor is there compelling testimony in the same vein . . . ." (Determination, conclusion of law "D").

In light of this failure of evidence regarding the existence of such an agreement, we find petitioner's argument to be without merit.

We will next examine the significance of the Division's acceptance of the interest, along with a letter from petitioner stating that the payment was made in exchange for the abatement of penalties. Specifically, petitioner contends that the result which it sought to achieve by the payment of interest (i.e., the abatement of penalties) and the acceptance of this payment by the Division created an implicit agreement to abate the penalties and, therefore, the Division must honor this agreement. This argument appears to invoke the contract law principle of accord and satisfaction. We have been faced with this argument in Matter of Fahy (Tax Appeals Tribunal, April 5, 1990). In rejecting this argument as a basis for a compromise settlement, we stated:

> "[s]ections 171 eighteenth and eighteenth-a of the Tax Law provide specific procedures for compromising a tax deficiency with the Division. An accord and satisfaction is not among the formal or correct procedures for settling tax claims outlined in [these sections] (Matter of Patricia W. Heath, State Tax Commn., October 5, 1984; see, Bowling v. United States, 510 F2d 112, 75-1 USTC ¶ 9333, at 86,786). In fact, no theory founded upon general concepts of accord and satisfaction can be used to impute a compromise settlement of a tax case (see, Bowling v. United States, supra). The United States Tax Court has held that principles of accord and satisfaction from ordinary contract law simply do not apply to tax law (see, Colebank v. Commr., T.C. Memo 1977-046, 36 TCM 200, affd. without opinion 610 F2d 999, cert denied 449 US 953)" (Matter of Fahy, supra).

In light of this precedent, we find petitioner's argument to be without merit.

We turn now to petitioner's assertion that the Division has introduced no evidence which proves that a valid assessment for interest and penalties for the year at issue existed as of

February 17, 1991 (the date the interest was paid) and, therefore, the interest voluntarily paid by petitioner should be refunded.

The Tax Law clearly states that where a taxpayer files a report that concedes the accuracy of a change to its Federal return and this change creates a deficiency in its New York tax liability, "[the] deficiency . . . shall be deemed to be assessed on the date of filing such report" (Tax Law § 1082[a][2], emphasis added). In addition, the Tax Law states that interest and penalties are assessed in the same manner as the tax (Tax Law §§ 1084[f], 1085[h]). These provisions are significant because where tax, interest, and penalty are self-assessed by virtue of a report of Federal changes, the taxpayer is not entitled to petition rights (cf., Tax Law § 1081[b], [c] [petition rights are provided where the Division initiates the assessment process by issuing a Notice of Deficiency]). Therefore, at the moment petitioner filed its report of Federal changes on December 21, 1989, it was assessed for the additional tax due, as well as for penalties and interest arising from this assessment of tax (Tax Law §§ 1082[a][2], 1084[f], 1085[h]).

Petitioner makes much of the fact that the Division failed to introduce a copy of the Notice and Demand which the Administrative Law Judge found to be issued on November 20, 1990 (Petitioner's brief, pp. 2-9, 11, 12). Petitioner asserts that the Division's failure to produce the notice supports its claim that the notice was never sent or received. We conclude, however, that regardless of whether a Notice and Demand was issued, petitioner would still not be entitled to refund of the interest paid. The lack of a proper Notice and Demand does not invalidate an assessment, but rather, merely prevents the government from utilizing its statutory collection powers in obtaining the tax owed; it does not require that monies paid by the taxpayer be refunded (see, Tax Law § 1092; Blackston v. United States, 778 F Supp 244, 91-2 USTC ¶ 50,585 [DC Md]; In re Dewberry, 158 BR 979, 93-2 USTC ¶ 50,562 [Bankr. WD Mich).[7]

[7]We also note that petitioner's assertion that no Notice and Demand was issued is at odds with its hearing reply brief, in which petitioner embraces a procedural chronology which includes the issuance of a Notice and Demand for interest and penalties on November 20, 1990 (Petitioner's hearing reply brief, pp. 4-5). In light of this implicit acknowledgement of receipt, we agree with the Administrative Law Judge's finding that petitioner was issued a

We will next address petitioner's argument that it is entitled to a second Notice of Deficiency for the interest paid on February 27, 1991 in light of the July 19, 1990 Notice of Deficiency, which contained erroneous amounts. Specifically, petitioner takes issue with the Administrative Law Judge's statement that:

> "petitioner's claim that it would not have paid interest but would have awaited a Notice of Deficiency so that it could protest both interest and penalty ignores the fact that interest and penalties were already assessed at the time of petitioner's 'voluntary' payment and incorrectly assumes the Division would have been obligated to issue a Notice of Deficiency to petitioner [footnote omitted]" (Determination, conclusion of law "H").

In our view, this conclusion of the Administrative Law Judge is correct unless the July 19, 1990 Notice of Deficiency reduced the amount of the December 21, 1989 self-assessment. To determine the impact that the July 19, 1990 Notice of Deficiency had on the assessment of December 21, 1989, we look to the meaning of "deficiency" within the Franchise Tax. Tax Law § 1081(h) defines "deficiency" as "the amount of tax[8] imposed by [Article 9], less . . . (ii) the amounts previously assessed . . . as a deficiency" (emphasis added). As stated earlier, the interest and penalties arising from petitioner's Federal changes were assessed on December 21, 1989 upon petitioner's filing of the report of Federal changes (Tax Law §§ 1082[a][2], 1084[f], 1085[h]). Moreover, it is undisputed that the interest and penalties included on the July 19, 1990 Notice of Deficiency referred to those amounts arising as a result of the same report of Federal changes. Because these interest and penalty components were previously assessed, they are, by definition, excluded from any subsequent deficiencies (see, Tax Law § 1081[h][ii]). Therefore, the July 19, 1990 Notice of Deficiency failed to assess any amounts not previously assessed and does not constitute a deficiency. Thus, we conclude that said Notice does not entitle petitioner to a new Notice of Deficiency for the interest paid.

Notice and Demand.

[8]Any reference to tax imposed by Article 9-A is deemed to also refer to applicable interest and penalties (Tax Law §§ 1084[f] and 1085[h], respectively).

Finally, we turn to the question of whether petitioner has established that its actions in this case do not warrant the imposition of penalties. Because the Administrative Law Judge has adequately and correctly addressed this issue, and petitioner has not set forth any additional reasons why penalties have been incorrectly imposed, we sustain the penalties based on the determination of the Administrative law Judge (Determination, conclusion of law "K").

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Schenectady Turbine Services, Ltd. is denied;
2. The determination of the Administrative Law judge is affirmed;
3. The petition of Schenectady Turbine Services, Ltd. is denied; and
4. The Notice of Deficiency dated April 19, 1991 is sustained.

DATED: Troy, New York
February 24, 1994

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner