

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

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| In the Matter of the Petition | : | |
| of | : | |
| FRANK J. AND KATHLEEN CAMPAGNA | : | DECISION |
| for Redetermination of a Deficiency or for Refund of | : | DTA NO. 818567 |
| Personal Income Tax under Article 22 of the Tax Law | : | |
| for the Year 1997. | : | |

Petitioners Frank J. and Kathleen Campagna, 180 Mill Road, Red Hook, New York 12571, filed an exception to the determination of the Administrative Law Judge issued on October 17, 2002. Petitioners appeared by Jeremiah F. Manning, Esq. The Division of Taxation appeared by Mark F. Volk, Esq. (Margaret T. Neri, Esq., of counsel).

Petitioners filed a brief in support of their exception. The Division of Taxation filed a letter in lieu of a formal brief in opposition. Petitioners did not file a reply brief. Oral argument, at petitioners' request, was heard on July 9, 2003 in Troy, New York.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUES

I. Whether the Division of Taxation had a rational basis for the issuance of the subject Notice of Deficiency and whether, under the instant circumstances, the Division of Taxation bore the burden of proof.

II. Whether petitioners have shown entitlement to a refund of economic development zone wage tax credits and economic development zone investment tax credits as claimed on their 1997 personal income tax return.

FINDINGS OF FACT

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

On September 25, 2000, the Division of Taxation (“Division”) issued to petitioners, Frank J. and Kathleen Campagna,¹ a Notice of Deficiency which asserted \$17,973.00 in additional tax due, plus interest, for the year 1997.

On his timely filed 1997 New York resident income tax return, petitioner claimed a refund of \$1,473.00 in economic development zone (“EDZ”) investment tax credits and \$16,500.00 in EDZ wage tax credits as his pro rata share of the credit base of Tri-State Associated Services, Inc. (“the corporation”), an S corporation wholly owned by Mr. Campagna.

The Division initially paid the refund claimed in petitioner’s 1997 return. Later, the return was audited and the Division concluded that, while petitioner was entitled to claim EDZ investment tax and wage credits, he was not eligible to receive a refund of those credits in lieu of carrying the credits forward to the next taxable year. Accordingly, the Division issued the September 25, 2000 Notice of Deficiency, asserting that petitioner was not entitled to the previously refunded \$17,973.00 in EDZ tax credits.

¹ Kathleen Campagna is a petitioner in this matter solely because she filed a joint return with her spouse, Frank J. Campagna, for the year at issue. Accordingly, all references to “petitioner” in this determination shall refer to Frank J. Campagna unless otherwise indicated.

Tri-State Associated Services, Inc., formerly known as Tri-State Copyland, Inc., was incorporated in New York in 1981 and was originally owned and operated by Mr. Campagna's mother. Mr. Campagna became the sole shareholder of the corporation by 1987.

Effective January 1, 1988, the corporation elected S corporation status for both Federal and New York State tax purposes. Such status remained in effect at all times relevant herein.

Tri-State Copyland, Inc. was a retail copy shop located at 608 Broadway, Kingston, New York. Its business was retail and included high-speed copying, color copying, and the sale of paper and office supplies. Its customer base was local.

In or about 1992, the corporation acquired property located at 71-81 Tenbroeck Avenue, Kingston, New York. This property was located in a manufacturing section of Kingston and the building located on the property required substantial investment to renovate and make suitable for the corporation's use.

In 1995, the corporation changed its name to Tri-State Associated Services, Inc.

Petitioner had a long-term plan for the corporation to change from a retail copy shop operation to a wholesale business of printing and binding short-run books. In or around 1995, petitioner began moving the corporation in that direction. In or about 1996 and in later years, the corporation invested in equipment which was installed in the Tenbroeck Avenue location. The corporation's largest equipment purchase was a Sakurai two-color press purchased for approximately \$350,000.00 in 1996. The corporation made other substantial purchases of equipment for use in the short-run book printing and binding operation. The corporation's employees received training to operate the new equipment.

The corporation's short-run book printing and binding business advertises nationally in trade publications. The customer base for this business consists of publishers, authors, and printers and is also nationally based.

In 1997, the corporation had employees in the Tenbroeck Avenue location involved in the printing of books.

During 1997 and 1998, the copy shop operation was ongoing at the 608 Broadway location. The corporation used the income from the copy shop operation to build the book printing and binding business.

The corporation obtained a Certificate of Eligibility for the New York State Economic Development Zones Program effective September 11, 1997. This certification made the corporation eligible to receive certain benefits, including EDZ tax credits, in connection with the facilities located at 608 Broadway and 71-81 Tenbroeck Avenue.

In 1998, the corporation completed a 3,500 square foot addition to the Tenbroeck Avenue premises for office space and storage. The corporation moved its offices from the 608 Broadway location to the Tenbroeck Avenue location during that year.

In 2000, petitioner unsuccessfully attempted to sell the retail copy shop at 608 Broadway by contacting other copy shop owners and placing a classified advertisement in the Poughkeepsie Journal. In 2001, the corporation sold the real property located at 608 Broadway.

Throughout the period at issue, the corporation had one set of books and records for both its retail copy shop and book publishing ventures. The corporation had one corporate identification number, one payroll and filed one tax return.

For worker's compensation purposes, in 1997 and 1998 the corporation had payroll totaling approximately \$145,000.00 classified under the copy shop category of "Printing: photostatic production." In 2000 and 2001, the corporation had payroll of about \$21,000.00 under this worker's compensation classification and about \$262,000.00 under the category for its book publishing business ("quick printing").

The corporation implemented a more complex computer and accounting system in 1997 or 1998.

For the first nine months of 2001, sales income from the short-run book printing and binding operation was 89 percent of the corporation's total sales.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge began his analysis by determining whether the Division had a rational basis for issuing the deficiency in this case. The Administrative Law Judge concluded that it did, in fact, have a rational basis since the corporation had been conducting business within New York State since its incorporation in 1981. The argument set forth by petitioners dealt with the refund of certain tax credits. As the Administrative Law Judge noted, where a tax credit is sought, it is petitioners who bear the burden to show entitlement to such credits. Thus, the Administrative Law Judge found that the Notice had a rational basis and that the burden of proof in this case properly fell upon petitioners.

The Administrative Law Judge next addressed whether petitioners were entitled to the tax credits sought by their refund claim. Preliminarily, after a thorough analysis of the applicable statute, the Administrative Law Judge noted that there was no dispute as to the corporation's eligibility to claim the EDZ credits at issue and that petitioners properly computed the

corporation's credit base with respect to the credits in issue. The instant dispute concerns whether the credits claimed by petitioners were refundable. The Administrative Law Judge noted that if the EDZ credits exceeded the taxpayer's tax for a given year, the excess may be carried over the following year or years and may be used to reduce the taxpayer's tax for such year or years. The Administrative Law Judge stated that if the taxpayer qualifies as "an owner of a new business" under section 210(12)(j) of the Tax Law, then pursuant to Tax Law § 606(j)(4) and (k)(5), the taxpayer may opt to claim a refund of such credit. Thus, the Administrative Law Judge distilled the case to whether petitioners have demonstrated that Mr. Campagna qualified as the owner of a new business such that they were entitled to a refund of the tax credits at issue.

The Administrative Law Judge emphasized that the corporation was incorporated in New York in 1981 and has been engaged in business in New York ever since. Thus, the Administrative Law Judge explained that the corporation was subject to tax pursuant to Article 9-A of the Tax Law for more than four taxable years prior to 1997. Therefore, the corporation did not qualify as a "new business" as defined in Tax Law § 210(12)(j)(3). Accordingly, the Administrative Law Judge determined that petitioner may not be treated as "an owner of a new business" and may not claim a refund of the EDZ wage tax credits and EDZ investment tax credits that are at issue herein.

The Administrative Law Judge rejected petitioners' argument that given the corporation's subchapter S election, the definition of "new business" as contained in Tax Law § 210(12)(j) does not apply because such an election treats the corporation as a pass-through entity and, thus, similar to a partnership, the definition of "an owner of a new business" as contained in Tax Law § 606(a)(10) was applicable. The Administrative Law Judge stated that the Tax Law section

referred to by petitioners defines an owner of a new business with respect to an individual who is either a sole proprietor or a member of a partnership. The Administrative Law Judge emphasized that since petitioner is the sole shareholder of an S corporation, he is neither a sole proprietor nor a partner in a partnership.

Lastly, the Administrative Law Judge addressed petitioners' motion for costs in this case. The Administrative Law Judge denied the motion as premature since pursuant to Tax Law § 3030 there had not been a final administrative determination made in this case. Petitioners did not file an exception with respect to this issue.

ARGUMENTS ON EXCEPTION

In their exception, petitioners continue to maintain their primary argument that the burden of proof in this case rests entirely on the Division and that the Division has not established a rational basis for the issuance of the Notice of Deficiency to them in the first instance.

Petitioners claim that they filed a tax return which sought a refund of certain tax credits. The Division received the return and issued them the refund requested. Petitioners state that, subsequently, the Division determined that petitioners were not entitled to the refund of the credits and it issued a Notice in the amount of the refund previously authorized. Petitioners assert that since the Division rescinded their claim for refund, this action taken by the Division necessitates that the burden of proof be appropriately upon the Division to prove that there was a right to rescind an already granted refund.

Moreover, petitioners argue that the subchapter S corporation qualified for and was granted a Certificate of Eligibility by the State of New York which entitled the corporation to certain tax credits for its participation in the economic development of the State. Petitioners

continue to assert that the partnership provisions apply to this case and “as a matter of law, the [Division] has the burden of proof when it rescinds an authorized refund” (petitioners’ brief in support, p. 3).

In opposition, the Division states that the Administrative Law Judge properly applied the law to the facts in the case and properly sustained the Notice of Deficiency issued to petitioners. The Division maintains that there is no evidence in the record to establish petitioners’ contention that a new business was created in 1997 that was separate and apart from the retail office supply and copy business that had been operating since 1981. The Division emphasizes that there was one certificate of incorporation, one corporate name and one set of corporate books and records. Thus, the Division respectfully requests that petitioners’ exception be denied in its entirety.

OPINION

We find that the Administrative Law Judge adequately and correctly dealt with the issues presented to him and petitioners have not advanced any new arguments which require us to modify the determination in any respect. Thus, we affirm the determination of the Administrative Law Judge for the reasons set forth therein.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Frank J. and Kathleen Campagna is denied;
2. The determination of the Administrative Law Judge is sustained;
3. The petition of Frank J. and Kathleen Campagna is denied; and

4. The Notice of Deficiency dated September 25, 2000 is sustained.

DATED: Troy, New York
January 8, 2004

/s/Donald C. DeWitt

Donald C. DeWitt
President

/s/Carroll R. Jenkins

Carroll R. Jenkins
Commissioner