STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
BROOKE-BOND GROUP (U.S.), INC.	:	DETERMINATION DTA NO. 810951
for Redetermination of a Deficiency or for Refund of Corporation Franchise Tax under Article 9-A of the Tax Law for Fiscal Year Ending June 30, 1988.	:	

Petitioner, Brooke-Bond Group (U.S.), Inc., c/o Unus Tax Department, 800 Sylvan Avenue, Englewood Cliffs, New Jersey 07632, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for fiscal year ending June 30, 1988.

A hearing was held before Carroll R. Jenkins, Administrative Law Judge, at the offices of the Division of Tax Appeals, Riverfront Professional Tower, 500 Federal Street, Troy, New York, on January 24, 1994 at 1:15 P.M. The last date for the filing of briefs was May 16, 1994. All briefs were filed within the prescribed time period. Petitioner appeared by its duly appointed attorney and representative, Douglas J. McCormack, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Robert J. Jarvis, Esq., of counsel).

The attorneys for the parties executed a stipulation of facts to be incorporated into the record.

ISSUES

I. Whether petitioner's New York State net operating loss deduction carried forward from 1980 and 1981 to fiscal years ending 1986, 1987 and 1988 was properly computed by the Division of Taxation.

II. Whether the New York State net operating loss deduction for a given year may be less than the Federal net operating loss deduction taken for the same year.

FINDINGS OF FACT

The parties have stipulated to the issues and the agreed facts. That stipulation is incorporated herein together with other facts in the record.

Petitioner, Brooke-Bond Group (U.S.), Inc. (hereinafter, "petitioner"), is a holding company in New York City which performs management services for its subsidiaries.[1] Petitioner's fiscal year ends June 30th. Reference herein to any of the subject tax years refers to a fiscal year ending June 30th.

The parties agree that petitioner had New York State entire net income (loss) before application of any New York State net operating loss ("NYS NOL") deductions, carrybacks or carryforwards for the years 1980, 1981, 1986, 1987 and 1988 as follows:

YEAR	ENTIRE NET INCOME AMOUNT
1980	$(1,313,905)
1981	(3,525,796)
1986	737,950
1987	1,860,269
1988	2,185,519

In the tax year ended June 30, 1981, petitioner had a Federal net operating loss ("Federal NOL") which it carried forward to subsequent

taxable years. For Federal purposes, petitioner did not use all of its Federal NOL carryforwards until June 30, 1988.

The parties agree that petitioner had Federal taxable income (loss) before application of any Federal NOL deductions, carrybacks or carryforwards, and was entitled to use its Federal NOL's as follows:

FYE	6/30/80	6/30/81	6/30/86	6/30/87	6/30/87
Federal Taxable Income Before NOL Deduction	$(1,845,321.00)	$(4,059,296.00)	$1,558,039.00	$1,864,595.00	$1,875,269.00
NOL Deduction					

[1]Petitioner's New York City address was not made part of the record.

1980 CB/CF[2] to 1977-1985	784,518.00				
1980 CF to 1986	1,060,803.00		(1,060,803.00)		
1981 CF to 1986		497,236.00	(497,236.00)		
1981 CF to 1987		1,864,595.00		(1,864,595.00)	
1981 CF to 1988		1,697,465.00			(1,697,465.00)
Federal Taxable Income after NOL	$ -0-	$ -0-	$ -0-	$ -0-	$ 177,804.00

The Division of Taxation ("Division") conducted a franchise tax audit ("the audit") of petitioner's business for 1988.

The NYS NOL deductions taken on petitioner's filed tax returns for 1986, 1987 and 1988 did not exceed the Federal NOL deductions taken by petitioner for the same years.

The Division and petitioner agree that Brooke-Bond was required to apply $784,518.00 of its NYS NOL for the tax year ended June 30, 1980 to income for the years 1977 through 1985, and that Brooke-Bond properly carried forward a NYS NOL deduction of $529,387.00 from 1980 to 1986, which deduction Brooke-Bond applied against its 1986 New York State entire net

income of $737,950.00, leaving a balance of New York State entire net income of $208,563.00 in 1986 before application of any other NYS NOL carryforward amounts (see, Finding of Fact "10").

The Division and petitioner disagree as to the manner in which the NYS NOL carryforward of $3,525,796.00 from the year ended June 30, 1981 should be applied in 1986, 1987 and 1988, respectively.

Petitioner computed its NYS NOL deduction for each of the tax years ended June 30, 1986 and June 30, 1987 as being equal to its entire net income for those years, respectively. As a result, petitioner carried forward $208,563.00 of its 1981 NYS NOL to 1986 and $1,860,269.00 of its 1981 NYS NOL to 1987. The remaining portion of the 1981 NYS NOL,

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[2] CB means carryback. CF means carryforward.

$1,456,964.00, was carried forward and applied to petitioner's 1988 entire net income of $2,185,519.00, leaving a balance in said entire net income of $728,555.00.

The following shows petitioner's calculations:

FYE	6/30/80	6/30/81	6/30/86	6/30/87	6/30/88
NYS Entire Net Income Before NOL Deduction	$(1,313,905.00)	$(3,525,796.00)	$737,950.00	$1,860,269.00	$2,185,519.00
NYS NOL Deduction					
1980 CB/CF to 1977-1985	784,518.00				
1980 CF to 1986	529,387.00		(529,387.00)		
1981 CF to 1986		208,563.00	(208,563.00)		
1981 CF to 1987		1,860,269.00		(1,860,269.00)	
1981 CF to 1988		1,456,964.00			(1,456,964.00)
NYS Entire Net Income after NOL	$ -0-	$ -0-	$ -0-	$ -0-	$ 728,555.00

Upon audit of petitioner, the NYS NOL deduction for fiscal years ending June 30, 1986 and June 30, 1987 was determined to be equal to the Federal NOL deduction taken for those years, respectively. As a result, the auditor carried forward $1,028,652.00 of petitioner's 1981 NYS NOL to 1986 and $1,864,595.00 to 1987. The remaining portion of the 1981 NYS NOL, $632,544.00, was carried forward and applied against petitioner's 1988 entire net income of $2,185,519.00, leaving a balance in entire net income of $1,552,975.00 (see below).

Division's Audit Computation FYE	6/30/80	6/30/81	6/30/86	6/30/87	6/30/88
NYS Entire Net Income Before NOL Deduction	$(1,313,905.00)	$(3,525,796.00)	$ 737,950.00	$1,860,269.00	$2,185,519.00
NYS NOL Deduction					
1980 CB/CF to 1977-1985	784,518.00				
1980 CF to 1986	529,387.00		(529,387.00)		
1981 CF to 1986		1,028,652.00	(1,028,652.00)		
1981 CF to 1987		1,864,595.00		(1,864,595.00)	
1981 CF to 1988		632,544.00			(632,544.00)
NYS Entire Net Income after NOL	$ -0-	$ -0-	$ (820,089.00)	$ (4,326.00)	$1,552,975.00

In the Division's view, the negative entire net income for 1986 and 1987 after applying the NOL deduction (Finding of Fact "11"), was lost and could not be carried forward to 1988 as a net operating loss.

As a result of the audit, the Division determined that petitioner was entitled to credit for overpayments in tax for 1986 and 1987. After giving credit for such overpayments, the Division issued a Statement of Audit Adjustment and a Notice of Deficiency to petitioner, both dated January 25, 1991, asserting additional corporation franchise tax due for fiscal year ending June 30, 1988 in the amount of $122,854.00, plus interest. As a result of the audit, Division also issued a Statement of Audit Adjustment and a Notice of Deficiency to petitioner, both dated January 25, 1991, asserting additional, corresponding Metropolitan Transportation Authority Surcharge for fiscal year ending June 30, 1988 in the amount of $20,885.00, plus interest.

Petitioner made a timely request for a conciliation conference with the Division's Bureau of Conciliation and Mediation Services. As a result of such conference, a Conciliation Order (CMS No. 111571), dated April 10, 1992, was issued to petitioner sustaining the statutory notices. Thereupon, petitioner filed a petition with the Division of Tax Appeals and the instant proceeding ensued.

SUMMARY OF THE PARTIES' POSITIONS

Petitioner and the Division agree on the amount of the NYS NOL available for carryforward from 1980 to 1986 ($529,387.00). The parties also agree as to the amount of NOL used as a deduction to Federal taxable income for 1986 ($1,558,039.00).

The disagreement in this case lies in whether petitioner's NYS NOL deduction claimed in 1986 can be less than the amount of petitioner's Federal NOL deduction in 1986.

Petitioner contends that when entire net income for a given year is smaller than Federal taxable income for that year before taking any NOL deductions, petitioner's NYS NOL deduction carried forward should not be required to be any larger than is necessary to reduce its entire net income to zero, even if that means its NYS NOL deduction is smaller than the

allowable Federal NOL deduction taken for the same year.

The Division argues that the law requires that the NYS NOL deduction for a given year must be the same as the allowable Federal NOL deduction, subject only to the limitations provided by the New York statute and regulations. This rule applies, says the Division, even if the NYS NOL carried forward for a given year results in a negative entire net income for the year carried to. In addition, says the Division, if after applying the NYS NOL to entire net income the resulting entire net income is reduced to a negative amount, that negative amount cannot be carried forward in future years as a net operating loss.

CONCLUSIONS OF LAW

A. The resolution of this matter is not a matter of numbers, it is a question of which party, the Division or the petitioner, has correctly interpreted the statute governing the application of the subject net operating loss deductions. If petitioner's interpretation prevails, its application of the subject NYS NOL deductions must be given effect. If the Division's interpretation of the statute, as codified in its rules and regulations, is rational, its application of those same NOL deductions, and the resulting tax asserted, must be sustained. Put another way, the decision as to which party has correctly interpreted the statute will govern how petitioner's NYS NOL from 1980 and 1981 should be applied and carried forward to 1986. The answer to that question will, in turn, govern the amount of NYS NOL petitioner will have available as a deduction against its 1988 income.

B. The interpretation of a statute by the agency charged with its enforcement is entitled to great weight (Matter of Howard v. Wyman, 28 NY2d 434, 322 NYS2d 683). To prevail, it is not sufficient for a petitioner to merely come forward with its own alternative interpretation of the statute, even if that interpretation is reasonable. Rather, a petitioner must demonstrate that the Division's interpretation of the statute is unreasonable or irrational, and that petitioner's interpretation is the only "reasonable" interpretation that can be drawn (Matter of Cove Hollow Farm v. State of New York Tax Commn., 146 AD2d 49, 539 NYS2d 127, 129; Matter of Sanjaylyn Co. v. State Tax Commn., 141 AD2d 916, 528 NYS2d 948, 950, appeal dismissed 72

NY2d 950, 533 NYS2d 55). Tax deductions depend upon clear statutory provisions therefor, and the burden is upon the taxpayer to establish a right to them (Matter of Grace v. State Tax Commn., 37 NY2d 193, 371 NYS 715).

C. Tax Law § 208.9(f) states, in pertinent part, that:

"A net operating loss deduction shall be allowed which shall be presumably the same as the net operating loss deduction allowed under section one hundred seventy-two of the internal revenue code [the corresponding Federal deduction] . . ., except that in every instance where such deduction is allowed under this article:

"(1) any net operating loss included in determining such deduction shall be adjusted to reflect the inclusions and exclusions from entire net income required by paragraphs (a), (b) and (g) hereof,

* * *

"(3) such deduction shall not exceed the deduction for the taxable year allowed under section one hundred seventy-two of the internal revenue code . . ." (emphasis added).

D. Section 3-8.2 of the Regulations states:

"(a) The net operating loss deduction allowed under article 9-A is presumably the same as that which is allowed for Federal income tax purposes, subject to the three limitations explained in subdivisions (b), (c) and (d) of this section.

"(b) The first limitation on the net operating loss deduction for purposes of article 9-A is that no deduction is allowed for a loss sustained during any taxable year beginning prior to January 1, 1961, or sustained during any year in which the corporation sustaining the loss was not subject to tax under article 9-A . . . .

"(c) The second limitation on the net operating loss deduction for purposes of article 9-A is that any net operating loss which is carried back or forward for Federal tax purposes must be adjusted to reflect the additions and subtractions required by sections 3-2.3 and 3-2.4 of this Part . . . .

"(d) The third limitation on the net operating loss deduction for purposes of article 9-A is that in any year, it may not exceed the deduction allowable for that year for Federal income tax purposes under section 172 of the Internal Revenue Code . . ." (emphasis added).

E. Section 3-8.5 of the Regulations provides:

"When the net operating losses of two or more years, or the portions of net operating losses of two or more years, are carried back or carried forward to be deducted from the income of one particular taxable year, the [Commissioner of Taxation and Finance] requires that an aggregate method of deducting the losses be used. The taxpayer must compute the aggregate of the Federal net operating losses to be carried to the particular taxable year, and, also, compute the aggregate of the net operating losses under article 9-A for such year.

"After computing the two aggregate figures, whichever of the two (Federal or State) is smaller is the aggregate net operating loss which is allowable as a carry back or carry forward to the particular taxable year. The limitations described in subdivisions (b), (c) and (d) of section 3-8.2 of this Subpart apply in deducting the aggregate of losses" (emphasis added).

F. Petitioner bases its argument on the language in Tax Law § 208.9(f) which states, in pertinent part, that:

"A net operating loss deduction shall be allowed which shall be presumably the same as the net operating loss deduction allowed under section one hundred seventy-two of the internal revenue code . . . except that in every instance where such deduction is allowed under this article:

* * *

"(3) such deduction shall not exceed the deduction for the taxable year allowed under section one hundred seventy-two of the internal revenue code [the corresponding federal deduction] . . ." (emphasis added).

Petitioner says this statutory language only prohibits the NYS NOL deduction from being greater than the corresponding Federal deduction, it does not prohibit it from being less. Thus, says petitioner, when entire net income is smaller than Federal taxable income before taking the NOL deductions, as in fiscal year ending June 30, 1986, it should be allowed to take a smaller loss for State purposes than it did for Federal purposes, thus being able to retain the unused loss to be carried forward in later years. Put another way, petitioner argues that it should not be required to use (carry forward) any more of its 1980-1981 NYS NOL to 1986 than is necessary to reduce its 1986 net income to zero, as long as this amount does not exceed the Federal NOL deduction for 1986.

G. The Division interprets Tax Law § 208.9(f) as requiring that Federal and State NOL amounts carried forward in a year must be the same amounts whether or not the resulting Article 9-A entire net income, after the NOL deduction, results in a negative amount for the carryforward year. Thus, says the Division, since petitioner carried forward a NOL loss of $1,558,039.00 from 1981 to 1986 for Federal purposes, petitioner must carry forward that same amount for State franchise tax purposes, even if that results in a negative entire net income, i.e., a loss of $820,089.00 for 1986. Under the Division's regulations interpreting Tax Law § 208.9(f), this negative entire net income (loss) of $820,089.00 cannot be carried forward as an

NOL loss in future years, i.e. 1988 (20 NYCRR 3-8.2, 3-8.5).

H. As set forth above, 20 NYCRR 3-8.5 deals with the aggregation of net operating losses. The regulations require that: (1) a taxpayer compute the aggregate of the Federal NOL to be carried to a taxable year; (2) compute the aggregate of the NOL under Article 9-A for such year; and (3) apply the smaller figure as the aggregate NOL which is allowable as a carryback or carryforward to the particular taxable year. Example 1 of this regulation demonstrates the point. In this example, Federal income for 1971 is $8,000.00 and the State income amount is $7,280.00. The Federal NOL deduction is $8,000.00, which reduces Federal taxable income to zero. The State NOL deduction is also $8,000.00, which reduces State taxable income (loss) to a negative $720.00. This $720.00 loss may not be carried back or forward as an NOL deduction (id., at footnote to Example 1; 20 NYCRR 3-8.2, footnote to Example 4).

I. The Division's regulations are consistent with Tax Law § 208(9)(f). That section provides, as noted, that a NOL deduction which a taxpayer is allowed in computing entire net income for purposes of Article 9-A shall be presumably the same as the NOL deduction allowed under Internal Revenue Code § 172. The Division interprets the term "presumably the same" as meaning "the same" subject only to the three limitations set forth in paragraphs (b), (c) and (d) of 20 NYCRR 3-8.2.[3] Case law would appear to support this interpretation of the term "presumably the same."

In Matter of Royal Indem. Co. v. Tax Appeals Tribunal (148 AD2d 845, 539 NYS2d 510, affd 75 NY2d 75, 550 NYS2d 610 [3d Dept 1989]), the court held that, in the calculation of a franchise tax assessment, NYS NOL deductions are limited to those amounts that are Federally "allowable" (see, Matter of American Employers' Ins. Co. v. State Tax Commn., 114 AD2d 736, 494 NYS2d 513; Matter of Eveready Ins. Co. v. New York State Tax Commn., 129 AD2d 958, 515 NYS2d 339, lv denied 70 NY2d 604, 519 NYS2d 1027; Telmar Communications Corp. v. Procaccino, 48 AD2d 189, 369 NYS2d 208; Matter of Lehigh Valley Industries, Tax Appeals Tribunal, May 5, 1988). The term "Federally allowable" has been interpreted as

[3]By its terms, 20 NYCRR 3-8.5 is also subject to the same three limitations.

meaning "the amount of the Federal deduction required to reduce Federal taxable income to zero" (Matter of Royal Indemnity Company, Tax Appeals Tribunal, February 19, 1988, citing Matter of Telmar Communication Corp., State Tax Commn., June 20, 1974, affd Telmar Communication Corp. v.

Procaccino, 48 AD2d 189, 369 NYS2d 208). In this case, the amount of the Federal NOL deduction required to reduce petitioner's Federal taxable income to zero was $1,558,039.00. Accordingly, this is also the amount that petitioner should have taken as a NYS NOL deduction for 1986.

J. Petitioner has not shown that its interpretation of the statute is the only reasonable interpretation, or that the Division's interpretation is irrational (Matter of Blue Spruce Farms v. State Tax Commn., 99 AD2d 867, 472 NYS2d 744, 745, affd 64 NY2d 682, 485 NYS2d 526). Accordingly, there is no basis for modifying the tax as computed by the Division.

K. Neither the statute nor regulations (Tax Law § 208[9]; 20 NYCRR 3-8.2, 3-8.5) carve out an exception or limitation that would permit a taxpayer whose NYS entire net income is less than its Federal NOL deduction in a given year, to take a NYS NOL deduction for that year that is lower than its Federal NOL deduction. The legislature could have made such provision. It did not.

L. The petition of Brooke-Bond Group (U.S.), Inc. is denied and the notices of deficiency dated January 25, 1991 are sustained.

DATED: Troy, New York
November 10, 1994

/s/ Carroll R. Jenkins
ADMINISTRATIVE LAW JUDGE