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IN THIS ISSUE

Despite Incorrect Advice from NYS Tax Department, Conference Request Held to Be Untimely
Page 1

Corporate Officer Liable for Sales Tax Despite Creditor's "Sweep Arrangement" with Corporation
Page 2

Charter Yacht Not Eligible for Commercial Vessel Exemption from Use Tax
Page 3

New York City Obtains Injunction Against Sale of Untaxed Cigarettes
Page 4

Insights in Brief
Page 5

EDITORS

Hollis L. Hyans
hhyans@mofo.com

Irwin M. Slomka
islomka@mofo.com

NEW YORK STATE + LOCAL TAX GROUP

Craig B. Fields
cfields@mofo.com

Paul H. Frankel
pfrankel@mofo.com

Hollis L. Hyans
hhyans@mofo.com

Mitchell A. Newmark
mnewmark@mofo.com

R. Gregory Roberts
rroberts@mofo.com

Irwin M. Slomka
islomka@mofo.com

Open Weaver Banks
obanks@mofo.com

Amy F. Nogid
anogid@mofo.com

Michael A. Pearl
mpearl@mofo.com

Richard C. Call
rcall@mofo.com

Ted W. Friedman
tfriedman@mofo.com

Nicole L. Johnson
njohnson@mofo.com

Kara M. Kraman
kkraman@mofo.com

William T. Pardue
wpardue@mofo.com

Rebecca M. Ulich
rulich@mofo.com

DESPITE INCORRECT ADVICE FROM NYS TAX DEPARTMENT, CONFERENCE REQUEST HELD TO BE UNTIMELY

By Hollis L. Hyans

In *Matter of Kevin Ryan and Paullina Simons*, DTA No. 824835 (N.Y.S. Tax App. Trib., Sept. 12, 2013), the New York State Tax Appeals Tribunal affirmed the dismissal of the taxpayers' petition by the Administrative Law Judge, and found that their request for a conciliation conference was untimely, since it had not been filed within the required 30-day period to contest an assessment containing a fraud penalty.

The Department issued a Notice of Deficiency to Mr. Ryan and Ms. Simons on October 19, 2011. Although there is generally a 90-day period from the date of mailing of a Notice of Deficiency to file a request for a conciliation conference or petition for a hearing, when a Notice asserts a fraud penalty, a request or petition must be filed within 30 days of the mailing of the Notice. Tax Law §§ 170[3-a][b], [h]. In accordance with that requirement, the Notice stated on its first page that any request for a conciliation conference or petition for a hearing had to be filed by November 18, 2011. The second page also advised that if a response was not received by November 18, the Notice would become an assessment subject to collection action. The request for a conciliation conference was not mailed until November 22, 2011.

However, before the issuance of the Notice in October 2011, on June 29, 2011, Mr. Ryan and Ms. Simons had received correspondence from the Department, incorrectly advising that they would have 90 days to request review of a notice by the Bureau of Conciliation and Mediation Services ("BCMS") or the Division of Tax Appeals. The petitioners therefore argued that they were confused by the different time limitations set forth in the June 29 letter and in the Notice, and that, because they relied to their detriment on the Department's statement of the time period in the June 29 letter, the Department should be estopped from denying them a hearing.

continued on page 2

The Tribunal set out the standard for estoppel against the government, which it found applied only in "unusual circumstances that would result in a manifest injustice to the private party." In order to invoke estoppel against the government, a taxpayer must demonstrate that a misrepresentation was made, and the government has reason to believe the party would rely on that misrepresentation; that the reliance on the misrepresentation was reasonable; and that the relying party acted to its detriment based upon the misrepresentation.

The Tribunal found that the first requirement was met: the June 29 letter was inaccurate and misleading when it clearly stated that the 90-day period would apply. The laws had changed a considerable period of time before the letter was written (in 2009 for the BCMS filing requirement, and in 2010 for the filing date in the Division of Tax Appeals), and therefore the issuance of the incorrect letter was found to be "arguably sufficiently 'reckless'… to give rise to the conclusion that the State should be estopped from enforcing the 30-day deadline."

However, the Tribunal went on to evaluate the second requirement for estoppel and determined that the petitioners' reliance on the June 29 letter was not reasonable, in light of both the statutory Notice, which explicitly provided the correct deadline, and the fact that the incorrect date in the June 29 letter is contradicted by express language in the Tax Law. Therefore, the Tribunal held that the petitioners failed to establish all of the grounds for estoppel against the Department. Their request for a conciliation conference was held to be untimely, and their petition was dismissed.

Additional Insights

Although the change in the statutory time periods for protesting Notices containing fraud penalties took effect, as the Tribunal noted, in 2009 and 2010, cases continue to arise in which this short deadline is missed. That is probably no surprise, since the facts in this case make it clear that even Department personnel have not all recognized that those changes were made. The 90-day general deadline for filing requests with either BCMS or the Division of Tax Appeals has been in place for more than 25 years, for cases that do not involve a fraud penalty, so the mistake may be understandable, but the onus is always on taxpayers to ensure that they understand and follow the jurisdictional time periods. While the *pro se* petitioners in this case may well have been confused by the conflicting advice they received, the burden when trying to assert estoppel against a government agency is extremely high. Here, even a letter found to have been "arguably reckless" was not sufficient to overcome the jurisdictional barrier.

CORPORATE OFFICER LIABLE FOR SALES TAX DESPITE CREDITOR'S "SWEEP ARRANGEMENT" WITH CORPORATION

By Irwin M. Slomka

A recent decision upholding the personal liability of a corporate officer for a corporation's New York sales tax liabilities is a stark reminder that such liability cannot be easily avoided, even when the corporation's creditors impede the officer's ability to pay the tax. *Matter of Patrick Kieran*, DTA No. 823608 (N.Y.S. Div. of Tax App., Sept. 12, 2013).

Personal liability for unpaid sales tax is imposed on any person required to collect and pay over the tax. Tax Law § 1133(a). This includes a corporate officer, director or employee who is "under a duty to act" for the corporation in complying with its sales tax obligations. Tax Law § 1131(1). A person authorized to sign a corporation's tax returns, or who is responsible for maintaining the corporate books or for corporate management, is generally considered to be "under a duty to act" and can be personally liable for the corporation's unpaid sales tax obligations. 20 NYCRR 526.11.

Patrick Kieran was the president of Bay Chevrolet, Inc., a now-defunct General Motors authorized car dealership previously located in Douglaston, Queens. Mr. Kieran had acquired the franchise partially with funds loaned by General Motors Acceptance Corporation ("GMAC"). GMAC also provided the financing for the company's car inventory purchases. As a condition for the financing, GMAC imposed a "sweep arrangement," under which it had access to the company's bank accounts that were used to, among other things, deposit customer payments, including sales tax collected from customers.

After Bay Chevrolet encountered financial difficulties, GMAC exercised its rights under the sweep agreement and collected what was due from the company directly from Bay Chevrolet's bank accounts, which included sales tax collected from customers. In addition, General Motors filed a motion terminating its dealer agreement, and thereafter Bay Chevrolet also granted GMAC of assignment of any proceeds from its open account with General Motors.

After Bay Chevrolet failed to file four consecutive quarterly sales tax returns and ceased operations, the Department issued estimated notices of determination to Mr. Kieran as a responsible officer of the corporation.

continued on page 3

In his capacity as president of Bay Chevrolet, Mr. Kieran was responsible for day-to-day operations and had full authority to, among other things, sign checks, tax returns and bank documents. However, he claimed he was not "under a duty to act" for the corporation allegedly because he did not have control over the payment of the corporation's taxes as a result of GMAC's "sweep agreement." In response, the Department claimed that Mr. Kieran "voluntarily" agreed to GMAC's seizure of the corporation's funds and therefore should be held personally liable.

The ALJ found that Mr. Kieran was "under a duty to act," since he displayed all of the necessary indicia of being a person responsible to collect the sales tax – e.g., control over financial affairs of the business, signing checks, and signing tax returns. The ALJ then rejected Mr. Kieran's argument that he did not have sufficient authority to pay taxes because the "sweep arrangement" gave GMAC control over Bay Chevrolet's bank accounts. According to the ALJ, having voluntarily entered into the agreement that allowed GMAC to, in effect, seize the company's bank accounts, Mr. Kieran could not now use that as a shield to avoid his statutory obligation to "protect the trust taxes." The ALJ cited to the Tax Appeals Tribunal majority decision in *Matter of Button*, DTA No. 17034 (N.Y.S. Tax App. Trib., Jan. 28. 2002), in which the Tribunal found that when corporate officers "voluntarily" granted a security interest and lien in the corporation's accounts to a creditor, the officers were not "precluded" from exercising their authority to pay the sales tax.

The ALJ did reject a sales tax assessment for a fifth sales tax quarter in which the taxpayer had received a Proposed Resolution at the Conciliation Bureau indicating a "zero" balance due for the quarter, and a Consolidated Statement of Liabilities also showing "zero" due, even though the taxpayer never agreed to the Proposed Resolution.

Additional Insights

It is clear that an otherwise responsible person cannot escape personal liability for sales tax by simply voluntarily surrendering his or her responsibilities. The line between what is truly "voluntary" and what is beyond that person's control, however, may not always be clear. It stands to reason that since most prudent lenders take security interests in the assets of corporate borrowers – with the security interests arguably also "voluntarily" given – the ALJ's rationale may have broad implications. The decision is a reminder to corporate officers that, regardless of a creditor's security interest in a corporation's assets, a responsible officer should make sure the security interest does not impede the business' ability to pay its ongoing sales tax obligations.

Regardless of a creditor's security interest in a corporation's assets, a responsible officer should make sure the security interest does not impede the business' ability to pay ongoing sales tax obligations.

CHARTER YACHT NOT ELIGIBLE FOR COMMERCIAL VESSEL EXEMPTION FROM USE TAX

By Kara M. Kraman

In *Matter of Stan Groman*, DTA No. 824274 (N.Y.S. Div. of Tax App., Sept. 12, 2013), a New York State Administrative Law Judge held that a yacht owner who claimed he hired his yacht out for charter trips between New York State and Canada was subject to compensating use tax on the market value of the yacht when it entered New York State.

In February 2004, while a resident of California, Stan Groman purchased a yacht, the "Bakes Gem," in Florida. Mr. Groman did not pay Florida sales tax on the purchase of the yacht because Florida has an exemption for vessels sold to nonresidents who remove the vessel from Florida. Shortly after purchasing the Bakes Gem, Mr. Groman retired to New York State, where he planned to operate a small charter business with the yacht out of Alexandria Bay, New York.

The Bakes Gem did not enter New York until May 1, 2005, after undergoing extensive repairs in New Jersey that winter. Shortly after entering New York waters, and before reaching Alexandria Bay, the Bakes Gem had an accident that necessitated an additional 16 months of repairs in Brewerton, New York. Finally, in June 2006, the Bakes Gem arrived in Alexandria Bay and began advertising and operating as a charter boat offering personalized charters either within New York or between New York and Canada in the St. Lawrence River and Thousand Islands region. Although Mr. Groman obtained a certificate of documentation from the United States Coast Guard, he did not register the vessel with the New York State Department of Motor Vehicles, and he did not pay New York State compensating use tax on the vessel.

In general, New York law imposes compensating use tax on the use within New York of tangible personal property purchased at retail, except to the extent sales tax has been or will be imposed. Tax Law § 1110(a). In cases in which the taxpayer can show that the property was used outside of the State for more than six months prior to entry into the State, the use tax

continued on page 4

is imposed on the basis of the current market value of the item at the time of its first use in the State, rather than its original sales price. Tax Law § 1111(b).

An exemption from New York State sales and use taxes exists for "[c]ommercial vessels primarily engaged in interstate or foreign commerce...." Tax Law § 1115(a)(8). The regulations specify that a commercial vessel is primarily engaged in interstate or foreign commerce "when 50 percent or more of the receipts from the vessel's activities" are so derived, and that interstate or foreign commerce is "the transportation of persons or property between states or countries." 20 NYCRR 528.9(a)(5).

In the case of the Bakes Gem, the ALJ determined that Mr. Groman did not meet his burden of proving it was a commercial vessel primarily engaged in interstate commerce. Specifically, the ALJ found that Mr. Groman's production of a mere three pages of the vessel's daily cruising log for 2006 only, and the affidavit of only one of several captains hired by Mr. Groman that some of the charters included locations in Canada, and little else, were insufficient to establish that the Bakes Gem was a commercial vessel that derived 50 percent or more of its receipts from interstate or foreign commerce.

[T]he production of a mere three pages of the vessel's daily cruising log for 2006 only, and the affidavit of only one of several captains...were insufficient to establish that the Bakes Gem was a commercial vessel that derived 50 percent or more of its receipts from interstate or foreign commerce.

The ALJ also held that the valuation of the Bakes Gem for use tax purposes was not its purchase price, but its market value on the date it was first used in New York, since the vessel had been used for more than six months outside of New York after its purchase. The ALJ held that the date of the Bakes Gem's first use in New York was on or about May 1, 2005, when it first entered New York waters, and not June 2006 when it arrived in Alexandria Bay after having undergone significant repairs, as Mr. Groman argued. The ALJ also held that the Department's proposed valuation, based on the average retail value of similar vessels in the first half of 2006, was reasonable in light of the taxpayer's failure to submit an appraisal or any professional valuation of the vessel.

Additional Insights

This case illustrates a common pitfall when sales tax is not paid on the purchase of a vessel or an aircraft (which are usually subject to similar rules). Several states either do not impose sales tax or provide sales tax exemptions for purchases of vessels and aircraft that are removed from the state within a certain amount of time. However, the state in which the vessel or aircraft is ultimately located will usually impose a compensating use tax on that property. Even if the owner does not register the vessel or aircraft in the state in which it is located, states often become aware of the presence of the vessel or aircraft within their borders when the Coast Guard, or in the case of aircraft, the Federal Aviation Administration, reports the vessel or aircraft to the state (as was done in this case). In New York, as in most states, had Mr. Groman paid Florida sales tax on his initial purchase of the vessel, he would have been entitled to a reduction of any use tax due and owing in New York equal to that amount.

NEW YORK CITY OBTAINS INJUNCTION AGAINST SALE OF UNTAXED CIGARETTES

By Hollis L. Hyans

In another case in the continuing efforts to eliminate sales of untaxed cigarettes, New York City successfully enjoined the sale of cigarettes shipped without payment of taxes, and without meeting the other requirements for tobacco sales, including identifying the contents of packages and obtaining age verification before delivery. *The City of New York v. Wolfpack Tobacco et al.*, No. 13 Civ. 1889 (S.D.N.Y. Sept. 9, 2013).

The law. Cigarette sales are subject to substantial state and city taxes, and their sale is highly regulated. New York State law requires that tobacco excise taxes be paid via a "stamp" that must be purchased in advance of sale and then affixed to each pack of cigarettes. Tax Law §§ 472, 473. Federal statutes, including the Cigarette Marketing Standards Act ("CMSA"), the Contraband Cigarette Trafficking Act ("CCTA") and the Prevent All Cigarette Trafficking ("PACT") Act, add substantial regulatory requirements, including (1) filing copies of invoices for shipped cigarettes with the states or localities to which they are shipped; (2) identifying the contents as tobacco on every shipping label; (3) forbidding delivery of more than 10 pounds of cigarettes in a single sale or shipment; and (4) requiring sellers to use a method of delivery that obligates the purchaser to sign for the delivery and provide proof of age. 15 U.S.C. §§ 376, 376a. These federal statutes explicitly allow local governments to obtain injunctive relief for violations of the statutory provisions.

The facts. A New York City investigator placed orders for cigarettes from Wolfpack Tobacco ("Wolfpack") and did not pay more than $34.45 for a carton, which meant that the cigarettes were untaxed, because New York State and City taxes alone amount to more than $50 per carton. The packages received by

continued on page 5

the investigator did not indicate that they contained cigarettes, the delivery driver did not request identification or proof of age, the packs of cigarettes did not bear tax stamps, and no reports were filed. The City also submitted evidence that the defendants had shipped thousands of packages weighing more than 45,000 pounds in total to customers in the City, all without identifying the contents as cigarettes and all without reporting to the State or City.

Holding. The District Court found that the City had met all of the requirements for issuance of a preliminary injunction. Since the Second Circuit has already held that a presumption of "irreparable harm" applies to injunctions under the CMSA and CCTA, and the court found that the same presumption should apply to the PACT Act, the City was entitled to a presumption of irreparable harm, one of the necessary components for issuance of a preliminary injunction. The City also demonstrated that it was likely to succeed on the merits, another requirement for issuance of a preliminary injunction. In fact, the court noted that Wolfpack's promotional materials indicated that packages would be left at the customer's address if no one was at home.

All of the defendants' arguments were rejected, including Wolfpack's position that it was not responsible for the failure of the delivery service to obtain proof of age, because the PACT Act puts the burden on the seller to use a method of delivery that requires age verification. The court also found that Wolfpack itself generated and applied the shipping labels, which not only failed to include the required notice identifying the contents as tobacco but instead represented that the packages contained "Native American Manufactured Products." While the defendants pointed out that neither of the two shipments actually sent to the City's investigator weighed more than 10 pounds, and that the shipment records introduced by the City did not conclusively demonstrate that any other particular shipment contained more than 10 pounds or in fact contained cigarettes, the court found that Wolfpack failed to introduce any contrary evidence in its own records of what it was shipping – if not cigarettes – in those packages. Since Wolfpack's primary business was the sale of tobacco, and its mailings offered free shipping for orders of more than 30 cartons as well as quantity discounts on orders of 40 to 59 cartons, and each carton weighs roughly two-thirds of a pound, the court found that it "strains credulity" to think that in dozens of shipments shown to weigh more than 10 pounds none contained more than 10 pounds of cigarettes.

Finally, the court found that the City had established that the violations were likely to recur, another requirement for the issuance of a preliminary injunction, and that the balance of the equities and the public interest favored the issuance of a preliminary injunction, given the findings by both Congress and the New York State Legislature of the dangers presented by remote sales of cigarettes.

Additional Insights

The defendants, in addition to contesting proof of violation, also raised the familiar argument that New York lacks the power to "'regulate the affairs of Indians on a reservation.'" However, the court quickly dismissed this argument, noting that the U.S. Supreme Court has held that, while sales of cigarettes to tribal members on reservations may not be taxed, states are free to tax sales to "'persons other than reservation Indians.'" *Dep't of Taxation and Fin. of N.Y. v. Milhelm Attea & Bros., Inc.,* 512 U.S. 61 (1994). It also rejected an argument that the CMSA conflicts with New York Indian Law § 6, which exempts reservation lands from taxation, finding that law only applies to taxes on real estate. The decision in *Wolfpack* thus joins other recent decisions uniformly upholding New York's right to require collection of its taxes on cigarettes from native vendors who sell to non-reservation consumers.

INSIGHTS IN BRIEF

Sale of Hotel Condo Units Not Subject to Mansion Tax

The sale of a condominium unit in a high-rise luxury hotel condominium in Manhattan for more than $1 million is not subject to the New York State "mansion tax." Based on various factors – including the real property tax assessment classification, Buildings Department retrictions and the hotel's restrictions on the owner's use of the condo units – the Department found that the units are not personal residences and are not subject to the "mansion tax" when sold. *Advisory Opinion*, TSB-A-13(4)R (N.Y.S. Dep't of Taxation & Fin., Aug. 30, 2013).

Department Proposes Regulations on Tax Return Preparer Requirements

On September 18, 2013, the Department published proposed regulations on the scope of tax return preparer registration requirements enacted in 2009. *Proposed Rulemaking*, N.Y.S. Dep't. of Taxation & Fin., "Tax Return Preparer Requirements," Part 2600 (N.Y.S. Register, Sept. 18, 2013). The proposed regulations implement several recommendations made in 2011 by a Task Force on Regulation of Tax Return Preparers. The proposed regulations set out the minimum qualifications for commercial tax return preparers who prepare New York State personal income tax returns, which include passing a New York State competency exam prior to preparing returns for compensation. There is a 45 day comment period for the proposed regulation.

Late Petition Permitted to Proceed Since Representative Was Not Served

In a trio of apparently related orders, a New York State Administrative Law Judge has held that a petition, despite having been filed on March 26, 2013, nearly a year after issuance of the Notice of Determination on May 29, 2012, was not untimely and could proceed to a hearing. *Matter of Angelo*

continued on page 6

Buffalino, DTA No. 825585 (N.Y.S. Div. of Tax App., Sept. 5, 2013); *Matter of Vincenzo Buffalino*, DTA No. 825584 (N.Y.S. Div. of Tax App., Sept. 5, 2013); *Matter of Alphonse Pesce*, DTA No. 825583 (N.Y.S. Div. of Tax App., Sept. 5, 2013). Although the Department of Taxation and Finance established through its mailing records, and an employee affidavit, timely and proper mailing of the Notice of Determination to the correct address for each petitioner on May 29, 2012, there was no evidence that the Department had mailed a copy of the Notice to the petitioners' representative, who had filed a Power of Attorney in February 2012. The ALJ noted that, while the statute does not expressly require service of a copy of a notice on a representative, the period for contesting an assessment is tolled if the taxpayer's representative is not served with a copy of the notice. *Matter of Hyatt Equities, LLC*, DTA No. 821447 (N.Y.S. Tax App. Trib., May 22, 2008).

Guidance Issued for Filings by Same-Sex Married Couples

Following the United States Supreme Court decision in *United States v. Windsor,* 133 S. Ct. 2675 (2013), striking down the ban on same-sex marriage in the Defense of Marriage Act, and Internal Revenue Service *Revenue Ruling 2013-17*, in which the IRS stated that it would recognize the validity of any same-sex marriage that is valid in the jurisdiction where it was performed, regardless of the couple's place of domicile, the New York State Department of Taxation and Finance has issued guidance for filing New York State personal income tax and estate tax returns by same-sex married couples. *Technical Memorandum*, TSB-M-13(5)I, (10)M (N.Y.S. Dep't of Taxation & Fin., Sept. 13, 2013). Couples who are in a legally recognized marriage and who filed as single or head-of-household for years before 2011 may file amended returns for all open years using a married filing status. For tax years 2011 and 2012, same-sex married couples are required to use a married filing status even if they used a single or head-of-household status for federal income tax purposes. The estates of individuals who were legally married to same-sex spouses, and who died prior to July 24, 2011 (the date New York's Marriage Equality Act took effect), may amend open estate tax returns as well.

continued on page 7