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Jurisdiction of Tribunals, Appellate Review

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This second in a series of articles on the two Tax Appeals Tribunals responsible for adjudicating tax controversies under the New York State and City tax laws will focus on the jurisdiction of the two Tribunals and appellate review of Tribunal decisions. Also, the recent decision by the City Tax Tribunal in the *U.S. Trust Corporation* case will be discussed.

Jurisdiction of Tribunals

The statutes creating the Tribunals set forth their jurisdiction to hear disputes between the State and City tax departments and taxpayers. The Tribunals are to provide fair hearings to taxpayers and ensure that due process requirements are met. The Tribunals are given the authority to rule on the validity of regulations (or in the case of the City, rules) issued under the tax laws by the Commissioners of the tax departments.

The City Charter [Search7RH168(a)] also provides that the City Tribunal, "shall have the same power and authority as the commissioner of finance to impose, modify or waive any taxes within its jurisdiction, interest thereon, and any applicable civil penalties." In *Matter of Alumet Corporation* (decided September 14, 1994 at fn. 22.), this provision was held to give the Tribunal authority to exercise the discretion of the Commissioner under the tax laws rather than giving deference to the Commissioner's exercise of such discretion.

This becomes very significant when a taxpayer objects to the use of the discretionary authority of the Commissioner (such authority is exercised frequently in the areas of combined returns and apportionment issues). Hence, a taxpayer need not prove an abuse of discretion by the City Commissioner, an exceedingly difficult standard, but rather can urge the City Tribunal to independently exercise such discretion using its own judgment and expertise.

A major limitation of the jurisdiction of the Tribunals is their inability to determine whether a tax provision is unconstitutional. Shortly after it started operating, the State Tax Appeals Tribunal decided in the *Matter of Fourth Day Enterprises, Inc.*, (decided October 27, 1988) that the "jurisdiction of this Tribunal, as prescribed in its enabling legislation, does not encompass such constitutional challenges. It is presumed that statutes are constitutional." However, in the *Matter of General Electric Company*, (decided March 5, 1992) the State Tribunal held that it had jurisdiction to find that a statute had been unconstitutionally applied. In that case, the State Tax Appeals Tribunal held that a sales tax on waste disposal service was not apportioned properly and, therefore, was unconstitutionally applied. Subsequently, the Tribunal stated "the hallmark of a question of the constitutionality of a statute as applied is that it depends for its resolution on specific facts, while the question of the facial constitutionality of a statute does not." *Matter of New Milford Tractor Co., Inc.* , (NYS Tax Appeals Tribunal, decided September 1, 1994).

This distinction puts a taxpayer in an awkward position; if he believes that the statute is unconstitutional on its face, redress cannot be had in the Tribunal; if the statute is facially valid but unconstitutionally applied, the Tribunal can make that finding and cancel the tax determination. In other words, if the law is clearly improper, the Tribunal cannot help you; but if the concept underlying the statute is permissible but is being improperly administered, the Tribunal process can result in an annulment of the tax assessment. A Supreme Court action for a declaratory judgement is an alternate means for contesting the constitutionality or inapplicability of a tax statute directly without the need to exhaust the administrative remedies.[(1)]

If a taxpayer raises constitutional issues in a CPLR article 78 appeal after a Tribunal decision, the Appellate Division said in *Matter of Capital Financial Corporation v. Commissioner of Taxation and Finance*, 218 A.D.2d 230 (3rd Dept., 1996) that it "will convert the matter to a combined proceeding pursuant to CPLR article 78 and an action for a declaratory judgment (see, CPLR 103[c])" without requiring the taxpayer first to bring a declaratory judgment action in Supreme Court.

Appellate Review

As mentioned in the previous article, the taxing authorities have no right to appeal adverse determinations issued by the Tax Appeals Tribunals, only taxpayers are afforded appeal rights. Taxpayers appeal from the State Tax Appeals Tribunal directly to the Appellate Division, Third Department and appeals from the City Tax Appeals Tribunal are heard in the Appellate Division, First Department. Such appeals must be commenced by proper service of the Notice of Petition and Petition upon the respondents and filing with the Appellate Division within four months after the Tribunal decision is rendered. Unlike other article 78 proceedings, no filings are made in the Supreme Court.[(2)]

Under the excise tax laws the taxpayer is required to post a bond to secure the payment of the amount determined to be due (including tax, interest and penalties) and costs and charges which may accrue in the proceeding prior to commencing the appeal.[(3)] Generally, the income tax laws provide that unless a bond is posted for tax, interest and penalty, the taxing authority is free to docket a warrant for the amounts due and proceed with collection activity. See, e.g. Tax Law Search7RHSearch7RH690(c) and 1090(c); N.Y.C. Search7RHSearch7RH11-529(c) and 11-681.3. A bond to cover costs is required to proceed with an appeal of income tax determinations. However, in *Matter of Morris Investors, Inc. v. Commissioner of Finance*, 69 N.Y.2d 933 (1987) (the author at that time represented the Office of the Corporation Counsel of the City of New York) it was decided that if the appropriate bond is not posted prior to commencement of the proceeding and the petition is dismissed for such failure, the taxpayer is permitted an additional six months after such dismissal to commence a new article 78 proceeding.[(4)]

In an Article 78 proceeding in the nature of *certiorari*, the question is whether a determination made as a result of a hearing held at which evidence was taken, is, on the entire record, supported by substantial evidence. There is a heavy burden on taxpayers to show that a determination is not supported by substantial evidence. The court in *Matter of Peterson Petroleum of New Hampshire v. Tax Appeals Tribunal*, 236 A.D.2d 752 (3rd Dept., 1997) said that, "we are not at liberty to substitute our judgment for a rational determination by the Tribunal that is supported by substantial evidence merely because it is possible to reasonably reach a different conclusion." The Court of Appeals in *Orvis Co. v. Tax Tribunal*, 86 N.Y.2d 165, 179 (1995) found substantial evidence to confirm a Tribunal decision where the "evidence supported a reasonable inference" for the conclusion reached by the Tribunal.

In areas in which the exercise of discretion is granted to the State or City Tax Commissioner, the courts have gone even further. The Court of Appeals in *Unimax Corp. v. Tax Tribunal*, 79 N.Y.2d. 139, 144 (1992) stated that the tax department's policy is "entitled to deference, provided it is not irrational or unreasonable, and does not contravene the specific legislative intent of the governing statute. . . . Deference is warranted even if a 'fairer' methodology . . . exists and could have been adopted." Also, in specific areas such as deductions and exemptions from tax, taxpayers have the extra burden of proving their entitlement to such benefits clearly and unambiguously[5].

The U.S. Trust Case

In the September 25,1997 article, the then pending case of *U.S. Trust Corp. and Subsidiaries* (decided November 25, 1997) was discussed. This closely-watched case involved the effect of New York City Charter Search7RH170(d), which provides that State Tribunal decisions are binding precedent on the City Tax Appeals Tribunal. A decision in favor of the taxpayer was issued by the City Tribunal.

The taxpayer contested determinations made after a joint audit by the State and City tax departments (the author was a Deputy Commissioner at the City's Department of Finance at the time of those determinations) requiring the inclusion of a Delaware subsidiary in its combined bank tax returns. The taxpayer was successful in contesting the State's determination before both the State Administrative Law Judge and the State Tax Appeals Tribunal. The City's Administrative Law Judge ruled against the taxpayer(before the State Tribunal decision was issued) after having reopened the record of the proceedings on his own motion and over objections to take additional evidence on the City's claim that the Delaware subsidiary itself had nexus to New York City and therefore was required to be included in the combined return.

The City Tribunal held that it was an abuse of the ALJ's discretion to re-open the record of the proceeding. The Tribunal cited its decision in *Matter of U.S. Life Realty Corp.*, (decided April 23, 1996) in which the Tribunal found that the ALJ had improperly "placed himself in the role of reinitiating and redirecting a completed audit. This is not a role the ALJ was meant to discharge by the Charter."

In the instant case, the hearing was re-opened more than two and one-half years after the close of the initial record. The City Tribunal found that the ALJ's re-opening of the record to resolve issues he did not think were adequately developed and after the record was long closed was an abuse of discretion. Because of that finding, the evidence admitted on the re-opened record was disregarded.

Once limited to the record made at the initial hearing sessions, the City Tribunal concluded that the facts adduced in the State proceedings did not contain "significant and material factual differences" from the City proceeding and therefore, "the facts before this Tribunal are not distinguishable from those that were before the State Tribunal". *U.S. Trust Corp.* at 50. The City Tribunal noted that it was immaterial that a different conclusion from that drawn by the State Tribunal could have been reached. Clearly, N.Y.C. Charter Search7RH170(d), referred to by the City Tribunal as a statutory rule of *stare decisis*, and the related doctrine of collateral estoppel, are intended to preclude re-litigating a matter even if there could be a difference of opinion between the two adjudicators on the outcome.

Finally, the City Tribunal left the door somewhat ajar as to how it will apply Charter Search7RH170(d) in the future. "How great a divergence in proof need be shown in order to support a departure from mandatory precedent (even though the parties, tax years, and even the audit results are identical) is a particularly vexing question." The City Tribunal did not reach that question and so it remains open for now. I expect

that this will be an ongoing issue as long as there are two separate Tribunals adjudicating the State and City tax laws.

[1] *GTE Spacenet v. New York State Department of Taxation & Finance*, 223 A.D.2d 468 (1st Dept., 1996); *R.J. Reynolds Tobacco Company v. City of New York Department of Finance*, 169 Misc. 2d. 674, aff'd. ___ A.D.2d ___ (1st Dept., December 9, 1997).

[2] *Matter of Leonard Spodek v. New York State Commissioner of Taxation and Finance*, 85 N.Y.2d 760 (1995).

[3] See, e.g. Tax Law Search7RHSearch7RH1138(a)(4) and 1411(a); N.Y.C. Admin. Code Search7RHSearch7RH11-708 and 11-2107.

[4] CPLR 205(a).

[5] *Mtr. of Grace v. NYS Tax Comm.*, 37 N.Y.2d. 193 (1975).