# Litigating a New York Tax Case, Volume 3: The Administrative Appeals Process

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The authors are doing a four-part series discussing all phases of litigating a New York tax case. In this third installment of the series, they cover the administrative appeals process within the New York State Division of Tax Appeals and the Tax Appeals Tribunal.

Our first two installments in this series covered the audit process[1] and conciliation conferences,[2] both of which are conducted under the umbrella of the New York Department of Taxation and Finance. Taxpayers who are dissatisfied with the outcome of the conciliation conference or who opt to forgo the conference altogether once the audit ends can bring their case before the Division of Tax Appeals and Tax Appeals Tribunal. This is when the case develops into true tax litigation, involving a new and very different set of rules and procedures from those that applied during the audit and conciliation conference. The merger of two very different and highly nuanced disciplines — tax law and civil procedure — present unique challenges in these cases. But it can also be a lot of fun.

In this article, we'll discuss the administrative appeals process before The Division of Tax Appeals and Tax Appeals Tribunal(collectively, the DTA).

## I. Overview of the Administrative Appeals Process

The DTA is a quasi-judicial body charged with "providing the public with a just system of resolving controversies" with the tax department.[3] The DTA is technically part of the tax department; however, it was created as an independent division over which the tax department's commissioner has no authority. Instead, the DTA is managed and administered by the Tax Appeals Tribunal's panel of three commissioners. Of course, since the division of taxation is one of the parties (that is, the taxpayer's adversary) in DTA proceedings, the tax department remains involved in the case throughout the administrative appeals process.

Proceedings before the DTA involve a two-level appeal process. The first level consists of an administrative hearing before an administrative law judge. This hearing is akin to a trial in tax litigation. After the hearing, the parties submit briefs; thereafter, the ALJ rules on the case by issuing a written determination. The ALJ's determination triggers a 30-day period for either party, or both, to file an exception with the Tax Appeals Tribunal to appeal the determination. Taking exception moves the case along to the second level of the appeal process, which is held before the Tax Appeals Tribunal.

Each year, more than 400 new cases are brought to the DTA. At the first level of the appeal before the ALJ unit, nearly half of the cases are settled before a hearing, according to recent statistics.[4] Of the cases that proceed to a hearing, the statutory notices are sustained — meaning the taxpayers lose — about 85 percent of the time.[5] The uphill battle continues at the second level before the Tax Appeals Tribunal, where roughly 60 cases were filed last year. Only a handful (six) were settled by the parties. And of the 27

[1]Timothy P. Noonan and Ariele R. Doolittle, "Litigating a New York Tax Case, Volume 1: The Audit Process," *State Tax Notes*, Feb. 29, 2016, p. 637.

[2]Noonan and Doolittle, "Litigating a New York Tax Case, Volume 2," *State Tax Notes*, Mar. 14, 2016, p. 797.

[3]Tax Law section 2000.

[4]Tax App. Trib., "Annual Report Fiscal Year 2014-2015," at 6, *available at* www.dta.ny.gov.

[5]*Supra* note 4, at 7.

decisions the tribunal handed down last year, the ALJ determinations were affirmed about 85 percent of the time, reversed less than 4 percent of the time, and modified or remanded about 11 percent of the time.[6]

But there's more behind those numbers. Many of the cases brought before the DTA involve fairly basic issues (such as late-filed appeals) in which taxpayers really had no shot of winning in the first place. And overall, as has been indicated in this space before, the tax appeals system in New York is one of the best in the nation — especially in terms of allowing taxpayers a full and fair airing of their disputes.[7] The judges are experienced tax professionals with deep knowledge of the tax law, the system works well, and taxpayers wanting their "day in court" may not like the result, but they will not be disappointed in the process.

## II. The Administrative Hearing Process

While the administrative hearing process is the first level of the DTA administrative appeal process, much transpires before the actual hearing is held. First, of course, the taxpayer must bring the case to the DTA by filing a petition. A few things to note before we dive in:

- First, the DTA's jurisdiction is limited to specific taxes, namely the taxes administered by the tax department. That includes state and local personal income taxes, corporate franchise tax, sales and use taxes, and a few others, but not estate tax or real property tax.[8]
- Second, the DTA can only adjudicate protests of statutory notices. That is, taxpayers must challenge a notice that affords them the right to a DTA hearing.[9] The term "statutory notice" encompasses a notice of deficiency, notice of determination, a denial of a refund or credit application, and a few others, but generally does not include notice and demands.[10] For these purposes, a conciliation order from the bureau of conciliation and mediation services is a statutory notice as well.
- Lastly, timeliness is critical. The most brilliant and carefully drafted petition will be dismissed if it is filed even one day late. There are no exceptions to this rule. Most statutory notices afford the taxpayer 90 days to file a petition; however, a shorter period sometimes applies.[11] Conversely, a longer period (two years) applies to a notice of refund disallowance in an income tax matter (but not for sales tax).[12]

With that said, we'll turn to the pleadings.

### A. The Pleadings

The pleadings generally consist of a petition (by the taxpayer), an answer (by the Division of Taxation), and sometimes a reply (by the taxpayer).

#### *1. The Petition*

The DTA proceeding begins when a taxpayer files a petition protesting a statutory notice. The petition is a Form TA-10, available on the DTA's website (www.dta.ny.gov). The petition is the first pleading filed in the case and once filed, the taxpayer becomes the petitioner.

Within the petition form, or in an attachment, the taxpayer must include "separately numbered paragraphs stating, in clear and concise terms, each and every error which the petitioner alleges has been made by the division, bureau or unit (for example, in issuing a notice of deficiency or in denying a refund application), together with a statement of the facts upon which the petitioner relies to establish each said error."[13] The best way to think about that document is to liken it to a formal complaint filed in a civil case. It should have the same look and feel, and it should be drafted with the same care lawyers take (or should take) when bringing a lawsuit in state or federal court.

Once the petition is received by the DTA, it is initially reviewed by the supervising ALJ to confirm that it is in proper form. If not in proper form, the petition is returned to the taxpayer for correction along with a "Notice of Intent to Dismiss Petition" (NOI), which is sent to both the taxpayer and to the would-be opposing counsel at the Division of Taxation's office of counsel. If not corrected within 30 days, the petition may be dismissed. That can happen for a variety of reasons, including defects in the petition, failure to enclose a statutory notice, or in the most common circumstance, when it appears that the petition was late filed. On issuance of the NOI, the parties are given 30 days to submit written comments on the proposed dismissal.

If the supervising ALJ deems the petition to be in proper form, the DTA sends the taxpayer or the taxpayer's representative a letter acknowledging receipt of the petition in proper form and assigns it a DTA number (akin to an index number). It then forwards a copy of the petition to the Division of Taxation's office of counsel to prepare its answer.

#### *2. The Answer*

The Division of Taxation is required to file its answer to the petition within 75 days of the date of the DTA's letter forwarding the petition, although a 15-day extension can be requested before the 75-day period expires. The answer must be filed with the DTA and served on the petitioner or

[6] *Supra* note 4, at 13.

[7] New York's tax appeals system received an "A" in a Council On State Taxation survey. *See* COST, "The Best and Worst of State Tax Administration" (Dec. 2013).

[8] *See* Tax Law section 171(2)-(6); Tax Law section 998; Tax Law section 2000; and Real Property Tax Law section 425(15)(b).

[9] Tax Law section 2008(1).

[10] *But see Matter of Grand Central JT VT*, DTA No. 82520, Tax App. Trib. (Mar. 10, 2016), in which the tribunal made clear that some notice and demands (there, a penalty-only notice and demand from an audit) are statutory notices that can be protested to DTA.

[11] Tax Law sections 2008(2) and 170(h), applicable to denials of licenses, issuance of fraud penalties, etc.

[12] Tax Law sections 689(c) and 1089(c).

[13] 20 NYCRR 3000.3(b)(5).

its representative within that time frame. In cases involving significant factual questions, missing that deadline can have drastic consequences for the division: All material allegations of fact in the petition are deemed admitted.[14] That actually arose in a case our firm handled many years ago, in which the ALJ issued a default order after the division's answer was filed 79 days late.[15] Reaching that outcome today is unlikely, though. When that case was decided in 1995, DTA's regulations authorized the petitioner to make a motion for a "determination on default" when the division's answer was filed late.[16] But that regulation was amended a few months later and now provides that "all material allegations of fact set forth in the petition shall be deemed to be admitted" when the division's answer is filed late.[17] Still, though, a late-filed answer can have consequences. And that's why we rarely see late answers anymore.

In most cases, the attorney filing the answer will be the division's point person on the case. As such, the petitioner can contact that person to discuss the case and should direct any correspondence sent to the division to that person's attention.

When the answer is received, we recommend marking up the filed petition as part of the hearing preparation, in order to understand exactly which of the allegations were admitted, denied, etc. Simply take a copy of your filed petition and mark in the margin next to each numbered paragraph "admits," "denies," or "DKI" for "denies knowledge or information sufficient to form a belief." Unless the pleadings are later amended, they are binding on the parties, so it is critical to know where your adversary stands.

#### *3. The Reply*

Within 20 days of being served with the division's answer, the taxpayer is entitled to respond by filing a reply. That is not something we do often, but because it is incumbent on the parties to give the DTA and each other "fair notice of the matters in controversy and the basis for the parties' respective positions,"[18] it may be necessary to respond to the division's answer. Thus, once a reply has been filed, or 20 days after the answer is served, the controversy is deemed "at issue" (that is, joined), and the case will be scheduled for a hearing.

### B. Motion Practice

Motion practice before the DTA is fairly limited, as compared with standard civil litigation. Some types of motions are specifically prohibited, including motions regarding the Civil Practice Law and Rules' discovery provisions and motions for costs or disbursements.[19] Motions for summary determination (which are akin to CPLR 3212 motions for summary judgment and governed by that provision) and motions to dismiss (which are governed by CPLR 3211) are the most commonly used motions. Making a motion requires a notice of motion stating the relief demanded and the grounds for such relief. We often include a memorandum of law with the motion as well.

### C. Other Procedural Tools

One of the most notable aspects of litigating cases at the DTA is the host of pre-hearing procedures and tools. Understanding how and when to use those tools is as critical to formulating a litigation strategy as it is to mounting a defense to the adversary's strategy.

#### *1. Stipulations of Fact*

Formal written stipulations can significantly shape hearing preparations, and have been used with some regularity in DTA litigation. Judges now expect that the parties will do their best to stipulate uncontested factual issues to ensure a more efficient hearing process.

#### *2. Demands for Bills of Particulars*

Either party can serve the other with a written demand for a bill of particulars demanding that the other supply additional details of the matters referred to in the pleadings. A bill of particulars provides an opportunity to get a clearer picture of the opponent's claims or defenses. It must be made within 30 days of the date the last pleading is served and contain a list of all of the items that need clarification. The party served must respond within 30 days, unless otherwise directed. Alternatively, the party served can move to vacate or modify the demand within 20 days of service. Refusing to respond or furnishing inadequate responses allows the demanding party to move for a preclusion order barring the non-responding party from introducing any evidence at the hearing regarding those items.[20]

#### *3. Admissions*

Admissions are used to compel a party to admit or deny some facts and can be particularly useful if the Division of Taxation is unwilling to enter into a stipulation of facts. At least 20 days before the scheduled hearing, either party can serve the other with a written request for admissions of the (i) authenticity of any papers or documents, (ii) correctness or fairness of photographs described in and served with the request, and (iii) truth of any other matter set forth in the request.[21] That process is used rarely, but it can be helpful to force the division into some sort of action to move the case forward.

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[14]20 NYCRR 3000.4(b)(4).

[15]*Matter of Biegler*, DTA No. 813170, Div. of Tax App. (June 15, 1995).

[16]20 NYCRR former 3000.4(a)(4).

[17]20 NYCRR 3000.4(b)(4); *see Matter of Cross Westchester Development Corp.*, DTA Nos. 815791 and 815792, Div. of Tax App. (Jan. 21, 1998).

[18]20 NYCRR 3000.4(a).

[19]20 NYCRR 3000.5(a).

[20]20 NYCRR 3000.6(a); *see Matter of Aquifer Drilling & Testing Inc.*, DTA No. 823592, Div. of Tax App. (Jan. 27, 2011).

[21]20 NYCRR 3000.6(b).

#### *4. Subpoenas*

A party seeking evidence in the possession of another party, or even a nonparty, may use subpoenas to compel the testimony or records sought. A *subpoena ad testificandum* can be useful when a party must rely on the testimony of witnesses who may be hesitant or unwilling to testify voluntarily. A *subpoena duces tecum* can be used to compel the production of books, papers, and other records at the hearing. Subpoenas can be issued by either the ALJ or counsel for a party.

Of course, there are limitations on the use of subpoenas. The subpoenaed party can request withdrawal or modification by filing and serving a request for the same on the party issuing the subpoena. The designated ALJ will then issue an order ruling on the request, which may be immediately appealed to the Tax Appeals Tribunal; thereafter, if necessary, the party can commence an action in Albany County Supreme Court to quash the subpoena.[22] Our position generally is that a taxpayer commencing such an action to quash a *subpoena duces tecum* cannot be compelled to comply with the subpoena at the hearing unless the court action is decided in favor of the Division of Taxation.[23]

### D. Pre-Hearing Activity

As the numbers reflect, many cases are settled without a hearing, so every effort should be taken to do so, especially given the time and expense of a formal hearing and subsequent appeals. The DTA's most recent annual report states that 48 percent of cases were settled by the parties.[24] Settlement discussions generally do not begin until the Division of Taxation files its answer, at which time the taxpayer learns who the department's attorney in the case will be.

After that, though, the parties usually have to wait several months before an ALJ is assigned to the case. But once a judge is assigned, a conference call is set with the judge and the parties to talk through the case, schedule the hearing, and the like. Sometimes there are a few calls before the hearing takes place. They serve a function beyond scheduling. In practice, we've found that those calls can jump-start discussions between practitioners and the division's counsel and start the process toward an amicable resolution.

### E. The Hearing

The DTA's formal hearings are held before ALJs, who oversee the presentation of evidence and resolve any administrative matters arising in the process. Taxpayers can elect to have the hearing held in Albany, New York City, or Rochester. Or taxpayers can elect not to hold a hearing at all, and instead handle the case "on submission," with all evidence submitted to the ALJ through the mail without live testimony. That option is obviously more cost-effective and is often the most efficient way to present a case to an ALJ. We have done it in several cases.[25] But take care when choosing that option. If there are important disputed facts, a live hearing with witness testimony is best.

#### *1. Hearing Memoranda*

Each party must file and serve a hearing memorandum at least 10 days before the scheduled hearing. It should contain a brief statement of the issues, a list of witnesses, a list of proposed exhibits, and a list of authorities relied on. Stipulations of fact, if any, should be enclosed. Though not required by DTA's regulations, some ALJs request that the parties share all exhibits before the hearing as well, usually with the submission of the hearing memos.

#### *2. Presenting the Case*

The hearing isn't a meeting. Nor is it an appeals conference. It is essentially a trial, and should be treated as such. There is testimony, exhibits, cross-examination, and the like. And with few exceptions, the taxpayer bears the burden of proof at the hearing. It is the taxpayer's day in court. There won't be any other chances. Make it count.

Most hearings begin with the division's counsel introducing jurisdictional papers — that is, the statutory notices, pleadings, any statute of limitations waivers, and so forth. Next, the division's attorney will state the issues in the case from their perspective. The taxpayer then has an opportunity to restate or otherwise respond and to make an opening statement. The hearing then proceeds with the taxpayer and the division presenting their cases through witnesses, documents, and the like.

Don't expect any *Perry Mason* or *My Cousin Vinny* moments at the hearing. There is no jury to play to. You are not putting on a show. And you won't score any points by making the auditor cry on the stand. Instead, practitioners should think of the hearing as an opportunity to set the table with every single important fact that is needed to win the case. Tell the story through the witnesses and evidence, and then pull it all together in . . .

#### *3. The Briefs*

After the hearing, the parties can — and should — brief their positions, and the taxpayer is entitled to submit a reply brief. Though not required, the taxpayer should *always* file a brief. It is the taxpayer's opportunity to tie up everything that transpired before and during the hearing and package it for the ALJ's consideration. The ALJ will certainly consider the briefs in deciding the case. Also, the briefs are part of the record on appeal.

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[22]20 NYCRR 3000.7.

[23]*See City of Los Angeles v. Patel*, 135 S. Ct. 2443 (2015); and U.S. Const., Amend. IV.

[24]Tax App. Trib., "Annual Report Fiscal Year 2014-2015," at 6, *available at* www.dta.ny.gov.

[25]*See Matter of Marriott International Inc.*, DTA Nos. 821078-85 and 821753, Div. of Tax App. (Nov. 26, 2008), *aff'd,* Tax App. Trib. (Jan. 14, 2010); *Matter of Luizza*, DTA No. 824932, Div. of Tax App. (Aug. 21, 2014), *rev'd,* Tax App. Trib. (Mar. 29, 2016); and *Matter of Falberg*, DTA No. 818960, Div. of Tax App. (Oct. 9, 2003).

***4. The Determination***

Once the ALJ receives the hearing transcript and all briefs and documentary evidence are submitted, the ALJ has six months to issue a determination. Up until then — from the audit, through the Bureau of Conciliation and Mediation Services process, and through the hearing — everything will have transpired outside the public eye, with all proceedings protected under taxpayer secrecy provisions. But once that ALJ decision is posted on the DTA's website, it's out there. The media will pick up important cases of interest, or cases involving interesting people. Make sure your client knows that going in. Some people don't like their tax disputes talked about on the back page of the *New York Post*.

## III. Review by the Tax Appeals Tribunal

Appeals of ALJ determinations are made to the Tax Appeals Tribunal. The taxpayer, the Division of Taxation, or both may appeal an adverse ALJ determination. And while determinations of ALJs do not have precedential value, the tribunal's decisions are precedential and become the law of the land unless the taxpayer has the decision overturned in a later court proceeding (to be covered in our next segment).

### A. The Exception

The party (or parties) appealing the ALJ determination must take exception within 30 days of the determination being appealed. The exception, filed using a notice of exception (Form TA-14), must state the (i) particular findings of fact and conclusions of law with which the party disagrees, (ii) grounds for the exception, and (iii) alternative findings of fact and conclusions of law. The exception must be filed and served on the adversary within 30 days of the ALJ determination, unless the tribunal grants an extension for "good cause." The exceptor must file and serve a brief to perfect the exception, and must do so either when filing the exception or, if so elected on the exception form, 30 days thereafter. The adversary then has 30 days to file and serve their own brief.[26]

### B. Oral Arguments

The exceptor may request an oral argument, as may the non-excepting party. However, if either party fails to make a timely written request, the opportunity for oral argument before the tribunal is lost. If oral argument is granted, the tribunal will advise the parties when and where oral arguments will be heard. When preparing for the oral argument, expect a hot bench. The tribunal's three commissioners are experienced in the tax law and interested in the cases before them.

### C. The Decision

The tribunal has *de novo* review authority, meaning it is not limited by findings of facts or conclusions of law by the ALJ. While the tribunal usually defers to the ALJ's evaluations witness credibility and evidentiary issues, it is not bound by the ALJ's determination of these matters. For that reason, the tribunal can entertain legal arguments that were not asserted before the ALJ; however, it will not review new facts or accept new evidence.[27]

The tribunal renders a written decision within six months of the exception (or six months of the date of the oral argument or the filing of briefs, whichever is later). In doing so, the tribunal has authority to rule on the validity of the tax department's regulations when those regulations are at issue. However, it cannot rule on the facial constitutionality of statutes.[28]

Tribunal decisions are not subject to further administrative review and, unless the taxpayer files a timely appeal, the tribunal's decision will "finally and irrevocably decide all the issues which were raised in proceedings before the division of tax appeals upon which such decision is based."[29] Therefore, as was the design, the tribunal's decisions are final and binding on the tax department, unless of course the department goes to the State Legislature and tries to get a tribunal decision retroactively reversed, which unfortunately happened in a recent case.[30] But absent that unusual situation, the tribunal's decisions are supposed to "finally and irrevocably" decide all issues under review.

## IV. Next Up

In the final installment of this series, we will talk about what happens when tax cases enter the New York state court system. I know — we can't wait either. ☆

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[26] 20 NYCRR 3000.17(a) and (b).

[27] *See Matter of Cano*, Tax App. Trib. (Dec. 12, 2002); and *Matter of Small*, Tax App. Trib. (Aug. 11, 1988).

[28] *See In re Allied Grocers Coop. v. Tax Appeals Tribunal*, 162 A.D.2d 791, 792 (3d Dep't 1990); *Matter of 52nd St. Designee Corp.*, Tax App. Trib. (Feb. 10, 2000);and *Matter of Fourth Day Enterprises*, Tax App. Trib. (Oct. 27, 1988).

[29] *See* Tax Law section 2016.

[30] *See Matter of Luizza*, Tax App. Trib. (Mar. 29, 2016); *see also Caprio v. New York State Dep't of Tax. & Fin.*, 25 N.Y.3d 744 (2015), *rearg denied* 26 N.Y.3d 955 (2015).