

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition :  
of :  
**UNIVISA, INC.** : DETERMINATION  
for Redetermination of a Deficiency or for Refund of : DTA NO. 820289  
Corporation Franchise Tax under Article 9-A of the Tax :  
Law for the Periods Ended December 31, 1996 and :  
May 16, 1997. :

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Petitioner, Univisa, Inc., c/o PricewaterhouseCoopers LLP, 1441 Brickell Avenue, Suite 1100, Miami, Florida 33131, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the periods ended December 31, 1996 and May 16, 1997.

On September 1, 2005 and September 12, 2005, respectively, petitioner, appearing by Kramer Levin Naftalis & Frankel LLP (Maria T. Jones, Esq., of counsel), and the Division of Taxation, appearing by Christopher C. O'Brien, Esq. (Nicholas A. Behuniak, Esq., of counsel), consented to have the controversy determined on submission without a hearing. All documentary evidence and briefs were submitted by February 8, 2006, which date began the six-month period for issuance of this determination. After due consideration of the record, Joseph W. Pinto, Jr., Administrative Law Judge, renders the following determination.

**ISSUE**

Whether petitioner is entitled to utilize certain net operating losses generated by an affiliated taxpayer in calculating its New York State entire net income for the taxable years ended December 31, 1996 and May 16, 1997.

**FINDINGS OF FACT**

The parties entered into a stipulation of facts containing 21 numbered findings, all of which, except paragraph “21”, have been incorporated into the Findings of Fact below. Paragraph “21” contained only a list of exhibits. In addition, the proposed findings of fact submitted by the Division of Taxation have also been incorporated into the Findings of Fact below.

1. During the years ended December 31, 1996 and May 16, 1997 (the “audit period”) petitioner did business in New York State and filed timely New York State general business corporation franchise tax returns (Form CT-3) pursuant to Article 9-A of the Tax Law.

2. Following a field audit, the Division of Taxation (“Division”) issued to petitioner a Notice of Deficiency, dated April 18, 2003, which set forth the following amounts of additional corporation franchise tax, penalty and interest due:

Period Ended	Tax	Interest	Penalty
12/31/1996	\$243,705.00	\$148,396.92	\$15,434.00
12/31/1996	40,420.00	24,612.68	2,560.00
5/16/1997	647,829.00	304,778.43	43,647.00
5/16/1997	<u>107,445.00</u>	<u>50,548.90</u>	<u>7,239.00</u>

	\$1,039,300.00	\$528,336.93	\$68,880.00
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The total tax, penalty and interest was \$1,636,615.93.

3. Following a conciliation conference in the Bureau of Conciliation and Mediation Services, an order was issued, dated September 10, 2004, which affirmed the Division's adjustments as reflected in the Notice of Deficiency.

4. Petitioner was incorporated in the State of Delaware on November 2, 1987 and was headquartered in Miami, Florida during the audit period. At that time, petitioner was owned indirectly by Grupo Televisa, S.A. de C.V. ("Televisa"), a Mexican corporation.

5. Petitioner filed consolidated U.S. corporation income tax returns (Form 1120) with its affiliated entities beginning with the year ended December 31, 1989, and including the audit period.

6. Petitioner began business in New York State on July 3, 1989 and began filing separate New York State general business corporation franchise tax returns beginning with the year ended December 31, 1989, and for each year of the audit period.

7. Petitioner reported net operating loss deductions on its Forms CT-3 in the amounts of \$42,903,847.00 and \$68,900,330.00 for the years ended December 31, 1996 and May 16, 1997, respectively.

8. Since January 1, 1989, Univisa Sports Holding Inc. ("USHI") was a wholly owned subsidiary of petitioner.

9. USHI filed as part of the federal consolidated group with petitioner for the years ended December 31, 1989, 1990 and 1991, and reported the following federal net operating losses ("NOLs") on a separate company basis per the federal consolidated return:

<b>Year</b>	<b>Amount of Net Operating Loss</b>
1989	\$2,401,789
1990	62,198,836
1991	<u>3,505,410</u>
<b>Total</b>	\$68,106,035

10. During the years ended December 31, 1989, 1990 and 1991, USHI's only business activity was its investment in a New York State partnership, The National American Sports Communication L.P. ("NASC"), which published a newspaper, The National Sports Daily, or "The National." USHI held a 50% interest in NASC.

11. USHI filed New York State general business corporation franchise tax returns beginning with the year ended December 31, 1989, and for each year of the audit period. For the years ended December 31, 1989, 1990 and 1991, USHI reported the following net operating losses to New York State:

<b>Year</b>	<b>Amount of Net Operating Loss</b>
1989	\$2,401,789
1990	62,198,836
1991	3,505,410
<b>Total</b>	<u>\$68,106,035</u>

12. Petitioner properly filed an election with its 1991 U.S. Corporation Income Tax Return to reattribute all of the losses sustained by USHI, as described above, to itself pursuant to Treasury Regulation § 1.1502-20(g)(1).

13. USHI did not conduct any business activities after 1991. For the taxable years ended December 31, 1992 and 1993, USHI filed New York State Forms CT-245 disclaiming tax liability and paying only a maintenance fee. Following the 1993 tax year, USHI no longer filed in New York State and was listed as inactive on Schedule 851 of the consolidated federal returns of Univisa, Inc. and subsidiaries through the taxable year ended May 16, 1997.

14. Petitioner's federal income tax returns for the years ended December 31, 1995 and 1996 and May 16, 1997 were audited, and subsequently, petitioner was permitted to use USHI's reattributed losses in the years which were audited.

15. Petitioner utilized the net operation losses reattributed from USHI to offset the income it reported on its New York State Corporation Franchise Tax Return for each of the years ended December 31, 1996 and May 16, 1997. The basis of the Notice of Deficiency issued to petitioner, more fully described in Finding of Fact "2", was the Division's disallowance of petitioner's use of USHI's net operating losses for these years.

16. The losses at issue were sustained during the years when petitioner and USHI were subject to tax under Article 9-A of the Tax Law.

17. The Division and petitioner resolved all issues in this matter with the sole exception of whether the net operating losses of USHI may be reattributed to petitioner for New York purposes. The parties also agreed that if petitioner prevails on this issue the tax portion of the assessment will be reduced to zero, and no additional penalty or interest will be due. If the issue with respect to USHI's net operating loss is decided in the Division's favor, the tax portion of the

assessment will be \$768,761.00 plus interest, but no penalty or penalty interest will be due and owing from petitioner.

***SUMMARY OF THE PARTIES' POSITIONS***

18. Petitioner contends that it properly elected to reattribute USHI's losses to itself pursuant to Treas Reg § 1.1502-20(g)(1) and as such, those losses became its losses on a separate company basis and part of its federal NOL, becoming the starting point for calculating the New York State NOL. Petitioner argues that the Division had no basis for making any adjustments or modifications to this amount. In fact, petitioner notes that there is no direct or implied provision of the law or regulations for a modification that mandates an add-back of reattributed NOLs.

19. Petitioner argues that since its election to reattribute USHI's losses to itself was a "deemed merger" pursuant to Treas Reg § 1.1502-20(g)(1) as a transaction described in IRC § 381(a), then New York's rules of treating actual mergers under the same section must apply, i.e., the losses of a merged entity may be used by the acquiring company. Petitioner points out that New York law provides that a successor corporation in an IRC § 381(a) transaction may utilize the NOL of a subsidiary that merged into it for the periods the subsidiary was taxable in New York State prior to the merger. Since the reattributed NOLs were generated during the period that USHI was taxable in New York, petitioner was entitled to use USHI's NOLs.

20. The Division contends that petitioner's reattribution of USHI's NOLs was predicated on the fact that it filed on a consolidated basis with USHI and that if petitioner filed on a separate basis for federal purposes it would not have been able to acquire the NOLs. Further, where a taxpayer files on a consolidated basis for federal purposes and on a separate basis for New York purposes, New York requires that the separate taxpayers compute their NOLs as if they were filing on a separate basis for federal income tax purposes.

21. In the alternative, the Division argues that since New York law requires that gains and losses attributed to subsidiary capital must be excluded from a taxpayer's net income, petitioner is not permitted to utilize the reattributed USHI NOL.

22. Petitioner counters that it did compute its NOL as if it were filing on a separate company basis when it completed a pro forma Form 1120 pursuant to the instructions for the Form CT-3. This pro forma Form 1120 indicated petitioner's NOL was calculated on a separate company basis and included the reattributed NOL and should be the starting point for determining petitioner's New York NOL.

23. Petitioner maintains that the reattributed NOLs are not losses attributed to subsidiary capital, but actual operational losses which were assumed by petitioner as if pursuant to an "actual" merger under IRC § 332 or a transaction to which IRC § 381 applies. No losses with respect to USHI's stock could be claimed in that instance. Rather, petitioner would succeed to the actual operational losses of USHI. Therefore, petitioner concludes that the losses are not attributable to USHI's stock and are not attributable to subsidiary capital.

#### *CONCLUSIONS OF LAW*

A. Tax Law § 208(9) provides that entire net income is the total net income from all sources, which shall be presumably the same as entire taxable income which a taxpayer is required to report to the United States treasury department. Tax Law § 208(9)(f) provides 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 . . . .(Emphasis added.)

As the Tax Appeals Tribunal stated in *Matter of Bausch & Lomb*

(Tax Appeals Tribunal, July 19, 1990):

The scheme of the statute is clear: the calculation begins with the allowable Federal deduction, this amount is adjusted for New York purposes, but the adjusted amount is limited to the allowable Federal deduction. (Citation omitted.)

For federal purposes, petitioner irrevocably elected to reattribute the losses of USHI to itself in a statement attached to petitioner's 1991 U.S. Corporation Income Tax Return, pursuant to Treas Reg § 1.1502-20(g)(1), which provides that "the common parent [herein petitioner] succeeds to the reattributed losses as if the losses were succeeded to in a transaction described under IRC § 381(a)." In turn, IRC § 381(a) provides that a corporation acquiring another corporation in certain liquidations and reorganizations may succeed to and take into account certain tax items of the distributor or transferor corporation (USHI), including net operating loss carryovers. (IRC § 381[a], [c].)

Therefore, pursuant to the provisions of Treas Reg § 1.1502-20(g)(1) and IRC § 381(a) and (c) petitioner acquired the losses of USHI upon its election to reattribute the losses made on its 1991 U.S. Corporation Tax Return as the common parent and as a separate entity, not as part of the consolidated group, and petitioner's NOLs, including the reattributed losses

of USHI, must be the starting point for the calculation of its New York NOLs.

B. The regulations at 20 NYCRR 3-8.1 provide, in part, as follows:

*A taxpayer is allowed a deduction similar to that allowed under section 172 of the Internal Revenue Code, or which would have been allowed if the taxpayer had not made an election under subchapter S of chapter one of the Internal Revenue Code, in computing entire net income for the purposes of article 9-A. A corporation which reports as part of a consolidated group for Federal income tax purposes but on a separate basis for purposes of article 9-A computes its net operating loss and its net operating loss deduction as if it were filing on a separate basis for Federal income tax purposes (20 NYCRR 3-8.1[a]; emphasis added).*

The instructions for Form CT-3, seeking compliance with this regulation, provide that filers that are members of affiliated groups for federal purposes must fill out a “pro forma” form 1120, reporting the federal taxable income that would have been required on a separate federal tax return and also attach to their return a copy of the federal consolidating workpaper indicating separate taxable income before any elimination of intercorporate transactions included in the federal consolidated return. That petitioner followed the instructions was not disputed by the parties. However, the propriety of petitioner’s inclusion of USHI’s NOLs in petitioner’s separate filing on the pro forma 1120 is disputed by the Division.

The Division, without any direct authority, contends that petitioner, as a separate taxpayer for federal purposes, could not have acquired the reattributed NOL from USHI, but could do so only as a member of the consolidated group. The Division's position is founded tangentially upon comments of the U.S. Department of the Treasury applicable upon the deconsolidation or disposition of stock of a subsidiary of an affiliated group. Specifically, the Division contends that when a reattribution election is made, the NOL remains part of the NOL of the consolidated group, not the parent, highlighting the difference between consolidated and separate return treatment. (**See**, 55 Fed Reg 9431.) However, it appears the Division has misinterpreted the language of the section it relies upon. The section clearly states at the outset that the parent may elect to reattribute the NOL carryover to *itself*, and that none of the carryover is apportioned to the subsidiary from which the NOL was reattributed. This mirrors the terms of Treas Reg § 1.1502-20(g)(1), which provides that "the common parent [herein petitioner] succeeds to the reattributed losses as if the losses were succeeded to in a transaction described under IRC § 381(a)."

In addition, there is further support in the federal regulations for finding that the NOL belongs to petitioner, as the parent corporation. Under circumstances where petitioner would leave or separate from the consolidated group upon a termination, it would be deemed the successor to USHI pursuant to Treas Reg § 1.1502-1(f)(4) (wherein the predecessor is referred to as the distributor or transferor, as in IRC § 381[a]).

For purposes of calculating the amount of consolidated NOLs, or CNOLs, to be carried over or back to separate return years, the federal regulations<sup>1</sup> provided that the amount of CNOL attributable to a member of the group is determined by multiplying the CNOL by a fraction, the numerator of which is the separate net operating loss of the corporation and the denominator of which is the sum of the separate net operating losses of all members of the group in such year having losses. Treas Reg § 1.1502-21(b)(2)(iv) states that for purposes of this calculation, “separate net operating loss of a member is determined by computing the CNOL by reference to only the member’s items of income, gain, deduction, and loss, including the member’s losses and deductions actually absorbed by the group in the taxable year . . . .” Therefore, the reattributed NOLs from

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<sup>1</sup>The same regulations in effect during the years in issue were Treas Reg former § 1.1502-79(a)(3) for 1996 and Treas Reg former § 1.1502-21T(b)(2)(iv) for 1997.

USHI are treated the same as petitioner's other losses, i.e., includible as part of its separate company losses for federal purposes and the proper starting point for calculating its New York NOL.

C. The Division gets little support from its reliance on the U.S.

Treasury Department's comments at 56 Fed Reg 47387, which appear to focus on the amount of the losses available for reattribution in a deconsolidation and safeguards against mismeasurement of the amount of the loss. In addition, the section echoes the discussion above, stating that under Treas Reg § 1.1502-20(g) the subsidiary whose losses are reattributed is treated as a predecessor whose reattributed losses are succeeded to by the common parent in a transaction described in section 381(a). In fact, the very situation is described in an example found in Treas Reg § 1.1502-20(g)(3)(iv) and lends support to petitioner's position.

D. The Division contends that, in order to place petitioner in the same position as if it were not part of a consolidated group, the acquisition and use of the reattributed USHI NOLs must be denied for New York tax purposes. This argument assumes that petitioner's calculation of its NOLs on a separate basis for federal purposes could not include the USHI NOLs. As discussed above, it is determined that petitioner was entitled to claim them.

The letter and spirit of the regulation at 20 NYCRR 3-8.1(a) - - a regulation meant to alleviate the inequity created when a taxpayer files a consolidated federal tax return and a separate New York State return - - sets the framework for calculating the NOL and NOL deduction. To the extent that the parties relied on ***Matter of Health-Chem v. State Tax Commn.***

(132 Misc 2d 941, 506 NYS2d 269) for anything other than its indirect reference to 20 NYCRR 3-8.1(a) and its meaning and intent, said reliance was misplaced. ***Health-Chem*** addressed the issue of whether the interest on refunds for net operating loss carry-backs had been properly calculated, not the reattribution of a subsidiary's NOL and the subsequent calculation of a parent's federal taxable income as reported on a separate federal tax return.

However, it is worth mentioning that petitioner raised a valid concern with respect to the "parity" that 20 NYCRR 3-8.1(a) aims to achieve. If the Division were to be permitted to ignore the reattribution election, a splitting of the NOLs would ensue, resulting in losses generated in New York not being utilized by any taxpayer. Simply, the reattributed losses would be utilized by petitioner at the federal level and would remain with the subsidiary for New York purposes. The subsidiary could not use the NOLs

at the state level because it has no federal losses. The result is anything but parity with taxpayers who file separately for both federal and state tax purposes.

E. The Division asserts that losses attributed to subsidiary capital must be excluded from entire net income. It reasons that the USHI NOLs are attributable to subsidiary capital and, therefore, must be excluded from petitioner's income. Since the analysis of the reattribution of NOLs from a subsidiary began with Treas Reg § 1.1502-20(g)(1), which provides that "the common parent [herein petitioner] succeeds to the reattributed losses as if the losses were succeeded to in a transaction described under IRC § 381(a) [merger or acquisition]" it follows that the focus is not upon the stock of the subsidiary but on the actual operational losses to which the transferee (petitioner) succeeds. Therefore, the reattributed NOLs cannot be characterized as losses attributable to subsidiary capital.

F. In ***Matter of Dreyfus Special Income Fund, Inc. v. New York State Tax Commission*** (72 NY2d 874, 532 NYS2d 356, 357), the Court of Appeals, citing the Appellate Division decision below, stated:

We have held, in interpreting a predecessor version of Tax Law § 208(9), that the term "presumably," as it appears in the statute, was not intended to afford respondent the freedom to vary the meaning of "entire net income" insofar as such income is equated

with the income a taxpayer reports to the United State Treasury (citation omitted).

For the reasons stated herein, it is determined that petitioner properly utilized the reattributed NOLs generated by USHI in calculating its New York State entire net income for the years in issue. The Division's attempt to vary the meaning of "entire net income" was likewise beyond the scope of its authority under the statute.

G. The petition of Univisa, Inc. is granted and the Notice of Deficiency dated April 18, 2003 is canceled, subject to the limitations agreed to by the parties as set forth in Finding of Fact "17".

DATED: Troy, New York  
August 3, 2006

/s/ Joseph W. Pinto, Jr.  
ADMINISTRATIVE LAW

JUDGE