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COURT OF APPEALS

STATE OF NEW YORK

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PHILIP CAPRIO AND PHYLLIS CAPRIO,  
Respondents,

-against-

No. 116

NEW YORK STATE DEPARTMENT OF  
TAXATION AND FINANCE, et al.,  
Appellants.

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20 Eagle Street  
Albany, New York 12207  
June 04, 2015

Before:

CHIEF JUDGE JONATHAN LIPPMAN  
ASSOCIATE JUDGE SUSAN PHILLIPS READ  
ASSOCIATE JUDGE EUGENE F. PIGOTT, JR.  
ASSOCIATE JUDGE JENNY RIVERA  
ASSOCIATE JUDGE SHEILA ABDUS-SALAAM  
ASSOCIATE JUDGE LESLIE E. STEIN  
ASSOCIATE JUDGE EUGENE M. FAHEY

Appearances:

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Official Court Transcriber

1 CHIEF JUDGE LIPPMAN: Number 116, Caprio.

2 (Pause)

3 CHIEF JUDGE LIPPMAN: Counselor, do you  
4 want any rebuttal time?

5 MS. VALE: Three minutes, yes, Your Honor.

6 CHIEF JUDGE LIPPMAN: Okay. Go ahead,  
7 counselor.

8 MS. VALE: May it please the court. Judith  
9 Vale for the State appellants.

10 CHIEF JUDGE LIPPMAN: Counselor, what's the  
11 test as to whether it can be retroactive or not?

12 MS. VALE: The test is the three-pronged  
13 balancing test from Replan and from James Square.

14 CHIEF JUDGE LIPPMAN: How does that test  
15 work in your favor?

16 MS. VALE: It works in our favor because we  
17 have a strong curative public purpose here for the  
18 retroactivity - - -

19 CHIEF JUDGE LIPPMAN: What's the curative  
20 public purpose?

21 MS. VALE: The pu - - - Baum - - - the pur  
22 - - - the purpose was - - -

23 CHIEF JUDGE LIPPMAN: Other than to get  
24 more money for the State; I get that.

25 MS. VALE: No, no, no, the main - - -

1 everything is clear that the main purpose here was  
2 because Baum and Mintz upset the settled law at the  
3 time.

4 CHIEF JUDGE LIPPMAN: So it's a curative  
5 purpose to say that - - - that you want to overturn  
6 the Mintz decision? That's curative?

7 MS. VALE: Yes, it's curative because up  
8 until Baum and Mintz - - -

9 CHIEF JUDGE LIPPMAN: I don't - - -

10 MS. VALE: - - - purchasers had - - -

11 CHIEF JUDGE LIPPMAN: I don't get that.

12 What's the theory that it could be curative?

13 MS. VALE: Because up until Baum and Mintz,  
14 purchasers were getting the asset-sale benefits, and  
15 nonresident sellers were paying the taxes. And then  
16 Baum and Mintz upset everything, turned it upside  
17 down, and suddenly purchasers didn't know if they  
18 were going to get to keep the asset-sale benefits  
19 that they had already been taking.

20 JUDGE STEIN: What is there to show us what  
21 was happening before Baum and Mintz? Because I think  
22 that's - - - that's really sort of the crux of this.

23 MS. VALE: Absolutely, Your Honor. I think  
24 it is very important to look at what was happening  
25 before Baum and Mintz, and all of the evidence in the

1 record shows that before Baum and Mintz, the State  
2 was taxing this and nonresident sellers were paying  
3 those taxes.

4 JUDGE ABDUS-SALAAM: But Judge Stein's  
5 question, counsel, is what is that evidence.

6 MS. VALE: Absolutely. You have the  
7 legislative findings; you have the legislative  
8 history. You have a public opinion in Haskell, from  
9 1997, saying that the deemed asset-sale gain passes  
10 through. You have Publication 88, also public in  
11 2006, saying that installment income under 453 - - -

12 JUDGE PIGOTT: Are there a lot of tax  
13 returns that you could point to where this was paid  
14 before, and all of a sudden, because of these two  
15 decisions, it didn't happen anymore?

16 MS. VALE: Yes, there - - - DTF estimated  
17 that there's going to be millions of dollars in  
18 refunds - - -

19 JUDGE PIGOTT: But before. In other words,  
20 you're saying people were paying this tax - - -

21 MS. VALE: Um-hum.

22 JUDGE PIGOTT: - - - they were paying it  
23 willingly, gladly, and were thrilled to be part of  
24 New York, and then these two decisions came out that  
25 said they don't have to pay it anymore, and they were

1 all upset. I'm kidding. But - - - and then, so now  
2 you've fixed it, so everybody's going back and paying  
3 the taxes. Is there proof that people were really  
4 paying the taxes beforehand?

5 MS. VALE: Yes, that's why there would be  
6 unintended refunds. I mean, there wouldn't be a  
7 refund possible - - -

8 JUDGE PIGOTT: I understand that.

9 MS. VALE: - - - unless people had paid the  
10 taxes. And DTF looked at this, and - - -

11 JUDGE RIVERA: But those - - - you're  
12 saying those refunds are pre-Baum and Mintz, or  
13 whatever that window would be?

14 MS. VALE: I - - - I don't know which one -  
15 - -

16 JUDGE RIVERA: Because post-Baum and Mintz,  
17 people might stop - - - or say that they want the  
18 refunds, right?

19 MS. VALE: Well, they're - - - they're  
20 probably post-Baum and Mintz, but the - - - some of  
21 the - - - I mean, in time, people would have sought  
22 the refunds after Baum and Mintz because that's what  
23 - - -

24 JUDGE RIVERA: Okay. That's what - - -

25 MS. VALE: - - - suddenly overturned the

1 law.

2 CHIEF JUDGE LIPPMAN: But that - - -

3 MS. VALE: But because the tax years stay  
4 open - - -

5 CHIEF JUDGE LIPPMAN: But that's different.  
6 That's the theory that yes, the State will get - - -  
7 will - - - will not lose money. You'll - - - you'll  
8 be able to - - - to get more revenue if you overturn  
9 Mintz, but - - - but again, curative means something.

10 MS. VALE: Yes, curative does mean  
11 something. But this court said, in James Square,  
12 that a main curative purpose is stopping unintended  
13 refunds. That is different - - - that is  
14 qualitatively different than seeking new money that  
15 you never expected to get. And the reason for that  
16 is because - - -

17 CHIEF JUDGE LIPPMAN: But unintended  
18 refunds, you mean in the future?

19 MS. VALE: Well, the tax years stay open  
20 for three years; I think that's the critical point  
21 here. So once Baum and Mintz hit and - - - and  
22 overturned settled law, people could seek refunds for  
23 - - -

24 JUDGE STEIN: That's the question.

25 MS. VALE: - - - prior years.

1                   JUDGE STEIN: How do we know that that was  
2 settled law? Because, clearly, Baum and Mintz said  
3 something. The question is, did Baum and Mintz say  
4 something that was really the practice all along, and  
5 nobody was saying anything about it, or did it change  
6 what was happening all along? How do we know what  
7 was happening before Baum and Mintz?

8                   MS. VALE: Absolutely. You look to, first  
9 of all, legislative findings, which specifically  
10 found that the settled practice was - - -

11                   JUDGE FAHEY: Well, let me - - - let's slow  
12 down there. Let's talk about that a second. Let's  
13 follow up on that, because the legislative amendment,  
14 as I understood this, the DTF statement as to the  
15 longstanding practices, those were actually - - -  
16 that amendment preamble was actually drafted by DTF,  
17 isn't that correct?

18                   MS. VALE: Well, DTF did seek this  
19 amendment because Baum and Mintz - - -

20                   JUDGE FAHEY: So - - - so they - - -

21                   MS. VALE: - - - had upset the law.

22                   JUDGE FAHEY: Okay. So they - - - they  
23 drafted it. Because I looked at it, and there wasn't  
24 any citation to any statute, regulation or DTF  
25 document, though that did come later. There weren't

1           any citations to the letter from the DTF Commission  
2           that Governor Paterson had commented on in the bill.  
3           And that's why, when we search the record, we're kind  
4           of struggling here to find out where in the record,  
5           as Judge Stein's original question was, points to  
6           something besides, you know, an argument or a  
7           rhetorical argument as to why this amendment should  
8           go forward.

9                         MS. VALE: Absolutely, Your Honor. And  
10           that's where you look to the other evidence, which is  
11           the public opinion in Haskell, in 1997, saying these  
12           deemed asset-sale gains pass through.

13                        JUDGE PIGOTT: Well - - -

14                        MS. VALE: And you look to Publication 88,  
15           also public - - -

16                        CHIEF JUDGE LIPPMAN: Judge - - -

17                        MS. VALE: Sorry - - -

18                        CHIEF JUDGE LIPPMAN: - - - go ahead.

19                        MS. VALE: - - - go ahead.

20                        JUDGE PIGOTT: But I wanted to go back to  
21           my original question, because I think I understand it  
22           now. You're saying that let's say a hundred people  
23           paid this tax, and they paid it because that's what  
24           the law was. All of a sudden, out come these two  
25           decisions, and since then, seventy of those one

1 hundred are coming back asking for refunds on this,  
2 that they had previously paid and had not - - - had  
3 no objection to. And that proves that this - - -  
4 these two decisions were clearly out of the - - - out  
5 of the norm - - -

6 MS. VALE: Yes, that's part of - - -

7 JUDGE PIGOTT: - - - and therefore - - -

8 MS. VALE: It's part of - - -

9 JUDGE PIGOTT: - - - therefore the curative  
10 aspect of it.

11 MS. VALE: Yes, that is part of the proof.

12 It's showing that, A, there was a lot of public  
13 information out there at the time, in 2007, saying  
14 the deemed asset sale pass through and that  
15 installment also pass through. And when you have  
16 other nonresident sellers actually paying the tax,  
17 back in 2007, it shows that the reasonable  
18 expectation in 2007 was that New York was treating  
19 these as deemed asset sales, both giving out the  
20 benefits of the deemed asset sale and collecting the  
21 taxes.

22 JUDGE READ: So they can have had no  
23 reliance? There's - - - you've talked about the one  
24 factor, the public purpose, but there are two others;  
25 one was the reliance and the other is the length of

1 time. Does this relate to the reliance too? You're  
2 saying they couldn't have relied on it because those  
3 - - - because of the 1997 decision?

4 MS. VALE: Yes. Yeah, it does relate to  
5 the reliance, because you - - - you don't have as  
6 much of a reasonable, settled reliance in immunity if  
7 all of the evidence at the time was suggesting that  
8 New York was going to tax these kinds of  
9 transactions. And reliance - - -

10 JUDGE STEIN: Can you distinguish the  
11 installment sales portion of it from the deemed asset  
12 sale, or do those two - - - have those two always  
13 gone together? Because it seems to me that the focus  
14 in this case, by the plaintiffs, is the installment  
15 issue, not necessarily the deemed asset sale,  
16 although they're a little connected.

17 MS. VALE: Yeah, I think it's a hard to  
18 break it apart. I mean, it's all part of one  
19 transaction that's happening at one time. And even  
20 back in 2007, it was clear that if you had  
21 installment, if you were delaying your gain through  
22 the 453, through the provision that plaintiffs rely  
23 on, it still had to pass through. We also think  
24 that's the most reasonable reading of prior law. But  
25 I think it's also shown that that was the way that

1 both DTF and other taxpayers were treating it back in  
2 2007.

3 And you can look at that PowerPoint from  
4 2002. There's actually a warning in there to  
5 auditors saying, people are trying to use the delay  
6 to make all of the deemed ass - - - to make that case  
7 a real asset sale, make all of that gain vanish, and  
8 suddenly not have to pay New York taxes. And so back  
9 in 2002, DTF was aware of this and was not allowing  
10 that kind of treatment. And it also just doesn't  
11 make sense. It doesn't make - - -

12 JUDGE ABDUS-SALAAM: I think your adversary  
13 or the plaintiffs here are saying that that might  
14 have been internal policy, but it wasn't public, that  
15 they couldn't have found that out, I guess,  
16 themselves. So what about this, with - - - the  
17 PowerPoint, for example, was internal, so what was  
18 public?

19 MS. VALE: Well, you have the Publication  
20 88, which says installment - - - with an S corp., if  
21 you have installment payments, they have to pass  
22 through and get reported on the shareholder's  
23 personal income tax. So you have that publication,  
24 and although the - - - the PowerPoint is an internal  
25 presentation, it's back in 2002, and it's to the

1           auditors who then go out and enforce this - - -

2                       JUDGE FAHEY:  Didn't the notes to the  
3           PowerPoint - - - weren't there something in the notes  
4           that was neg - - - and I've got language that - - -  
5           I'm looking at my notes here, "The gain would not be  
6           included in the numerator of the New York source  
7           fraction unless the nonresident shareholder's stock  
8           in the corporation is employed in another trade or  
9           business carried on in New York by the shareholder,"  
10          which is tracking the language of the exemption that  
11          the petitioners are relying upon.  And that was in  
12          the notes attached to the PowerPoint presentation.

13                      MS. VALE:  That piece actually is coming -  
14          - - coming out of the Haskell opinion; if you look at  
15          it, it's almost a cut and paste.  And that's talking  
16          about - - - it is talking about the liquidation piece  
17          that happens in all of these transactions.  A  
18          liquidation happens whether you delay the payment or  
19          not.

20                      JUDGE FAHEY:  You're saying you weren't  
21          relying on that, then?  That's not your  
22          interpretation of it, even though it was the notes in  
23          the PowerPoint presentation?

24                      MS. VALE:  Well, I think it's still - - -  
25          that note is still true when you're talking about - -

1 - I guess I have to - - - you have to break it down  
2 into the deemed asset sale and the liquidation, and  
3 we're saying that the deemed asset-sale portion that  
4 was calculated here - - - plaintiffs did a  
5 calculation for their deemed asset sale; you can see  
6 it in the record at pages 385 to 387. That portion  
7 of the gain still has to pass through. And that the  
8 delay of just delaying one month - - -

9 JUDGE STEIN: How about one day?

10 MS. VALE: Or day. It could - - - it could  
11 absolutely be a day. Under plaintiff's theory, that  
12 would make all of the deemed asset-sale gain just  
13 vanish, and suddenly assets that were used to do, in  
14 this case, fifty percent of the business in New York,  
15 all of a sudden there's no taxes at all.

16 JUDGE STEIN: Do you know how the federal  
17 tax, the IRS treats the deemed liquidation for tax  
18 purposes?

19 MS. VALE: We think that you have to look  
20 to the 453B to understand the federal treatment.  
21 That piece brings the whole treatment around full  
22 circle. And in 453B, it says both the shareholders  
23 and the corporation are getting the benefit of a  
24 delay, but once the shareholder recognizes gains or  
25 losses, you have to look to 1366(b), which is the

1 pass-through rules. So you have to still look back  
2 to the corporation to know which pots of money are  
3 coming from which source, so that the pot of money  
4 that was coming from the deemed asset sale should  
5 still pass through. That was how we understood  
6 federal law. We think that's the most reasonable  
7 reading of federal law, and it's the way that DTF and  
8 other taxpayers were treating these transactions back  
9 in 2007, which you can see from all of the evidence.

10 And I just want to point out - - -

11 CHIEF JUDGE LIPPMAN: Counselor - - -

12 MS. VALE: - - - they just have - - -

13 CHIEF JUDGE LIPPMAN: - - - finish your  
14 thought.

15 MS. VALE: Finish the thought. Plaintiffs  
16 had the burden here, and they produced no evidence to  
17 - - - to show that it would have been a reasonable,  
18 settled expectation, in 2007, to think you were going  
19 to get immunity.

20 CHIEF JUDGE LIPPMAN: Okay, counselor.  
21 Let's hear from the other side.

22 MR. NICOLICH: Thank you, Your Honor. John  
23 Nicolich, representing the Caprios, the - - -

24 CHIEF JUDGE LIPPMAN: Counsel, was it a  
25 reasonable expectation back in 2007?

1 MR. NICOLICH: The reasonable expectation  
2 that this was not taxable for many, many - - -

3 CHIEF JUDGE LIPPMAN: Based on what?

4 MR. NICOLICH: - - - reasons.

5 CHIEF JUDGE LIPPMAN: Based on what?

6 MR. NICOLICH: Because, as - - - as the  
7 State continues to say, it's supposed to be federal-  
8 state conformity. The federal statutes and the  
9 federal regulations clearly treat - - - this 338  
10 transaction, the purchaser gets to treat it as a sale  
11 of assets, but the regs make very clear that the  
12 seller continues to treat it as a sale of stock.  
13 It's considered a liquidation under the federal  
14 statutes. The statutes are very clear - - -

15 JUDGE STEIN: So are you talk - - - does  
16 this apply whether it's an installment sale or not?

17 MR. NICOLICH: That - - -

18 JUDGE STEIN: Or does it - - -

19 MR. NICOLICH: That applies whether it's an  
20 installment sale or not, correct.

21 JUDGE READ: And you rely for that on your  
22 interpretation of the federal law?

23 MR. NICOLICH: My interpretation - - - the  
24 regulations give examples and say that this is  
25 treated as a liquidation. And the federal statute

1 says a liquidation of a corporation is treated as a  
2 shareholder's sale of stock.

3 JUDGE READ: That's in the Revenue Code?

4 MR. NICOLICH: That's in the Revenue Code,  
5 and as the State points out in their briefs, there's  
6 supposed to be federal-state conformity - - -

7 JUDGE ABDUS-SALAAM: So your position - - -

8 MR. NICOLICH: - - - so we follow that  
9 principle.

10 JUDGE ABDUS-SALAAM: - - - is that you  
11 relied on the way the feds treated this to interpret  
12 how the State would treat it?

13 MR. NICOLICH: That's because that's  
14 exactly what the federal-state conformity requires.

15 JUDGE ABDUS-SALAAM: But you didn't think  
16 that - - - as the dissent in the Appellate Division  
17 pointed out, that it might have been important to get  
18 an opinion - - - a tax opinion from a lawyer or  
19 someone else to that effect?

20 MR. NICOLICH: The Caprios were  
21 well-represented at the time. This issue was never  
22 raised at the trial court, so we never had the  
23 opportunity to go in and put that kind of evidence,  
24 if that was something that was required.

25 JUDGE STEIN: I'm a little con - - - I wish

1           - - - I'd just like you to clarify something for me.  
2           In your complaint, you repeatedly refer to the tax on  
3           gain recognized on payments received from installment  
4           obligations.

5                         MR. NICOLICH: Correct.

6                         JUDGE STEIN: Does it matter whether this  
7           is a deemed asset sale or an asset sale or - - -  
8           that's - - -

9                         MR. NICOLICH: Well, it matters, because  
10          under the federal regulations that we followed, the  
11          regulations are directed to a 338(h)(10) transaction,  
12          and specifically gives an example of when that  
13          transaction is effected with an installment payment,  
14          and very clearly lays out, in example 10, that when  
15          the installment payment is made years later, it is  
16          treated as a payment for the sale of stock.

17                        JUDGE STEIN: But you're arguing that  
18          whether it's a day later or a year later, it doesn't  
19          matter what the transaction was; if there's now an  
20          installment payment, rather than an immediate  
21          payment, it changes the entire character of the sale  
22          and it's not taxable. Is - - -

23                        MR. NICOLICH: No, that's not quite right  
24          in two points.

25                        JUDGE STEIN: Okay.

1 MR. NICOLICH: First - - -

2 JUDGE STEIN: How am I wrong?

3 MR. NICOLICH: - - - in terms of the  
4 installment, you have to understand that when counsel  
5 says it was a day later or a month later, there  
6 actually were two payments here - - -

7 JUDGE STEIN: I understand that, but the -  
8 - -

9 MR. NICOLICH: - - - and one was done - - -

10 JUDGE STEIN: - - - the vast majority was  
11 one month after - - -

12 MR. NICOLICH: One month after.

13 JUDGE STEIN: - - - the deemed asset sale.

14 MR. NICOLICH: But the federal law, 453,  
15 requires - - - requires this circumstance, when  
16 there's a second payment, to be treated as an  
17 installment transaction, unless the taxpayer  
18 specifically elects not to. So the default is it's  
19 treated as a installment sale.

20 JUDGE STEIN: That begs the question: why  
21 would installment payments be treated differently?

22 MR. NICOLICH: And - - -

23 JUDGE STEIN: Why would it matter if it was  
24 the day be - - - the day of the - - - the sale or a  
25 month later? Why does that make a difference?

1 MR. NICOLICH: That's the way the law is  
2 written.

3 JUDGE RIVERA: Can I ask, what's the  
4 consequence of that, the federal level? What - - -  
5 how does that work - - -

6 MR. NICOLICH: On the federal - - -

7 JUDGE RIVERA: - - - for your client?

8 MR. NICOLICH: - - - level, the difference  
9 is there's a capital gains tax, so it gets capital  
10 gains tax treatment.

11 JUDGE RIVERA: All right.

12 MR. NICOLICH: That's - - - that's a  
13 difference there, and of course the payment of the  
14 tax is delayed for when - - - until when the  
15 installment payments are received.

16 Okay.

17 CHIEF JUDGE LIPPMAN: Counsel?

18 JUDGE FAHEY: So that's the real purpose of  
19 the installment payments? That's why they're  
20 structured that way, to deal with the capital - - -  
21 the capital gains problem?

22 MR. NICOLICH: And - - - under federal tax  
23 law, I believe they are. In - - - in this case - - -  
24 I mean, there were two reasons the - - - the - - -  
25 why this is not taxable. Both 338(h)(10), as Baum

1 and Mi - - - as Baum indicates, this is a sale of  
2 stock; sale of stock to nonre - - - by nonresidents  
3 are not taxable.

4 JUDGE FAHEY: Um-hum.

5 MR. NICOLICH: And - - - sorry, I lost my  
6 thought.

7 JUDGE FAHEY: Go ahead.

8 MR. NICOLICH: Okay.

9 JUDGE FAHEY: Don't let me throw you off.

10 JUDGE PIGOTT: Well, the big deal - - -  
11 your argument is due process. You're saying that the  
12 - - -

13 MR. NICOLICH: Yes, it's due - - -

14 JUDGE PIGOTT: - - - retroactive  
15 application of this is a denial of - - -

16 MR. NICOLICH: And this court has been very  
17 clear that in James Square, sixteen to thirty-two  
18 months retroactivity was improper - - -

19 JUDGE READ: So three and a - - -

20 MR. NICOLICH: - - - and violated due  
21 process.

22 JUDGE READ: - - - three-and-a-half years  
23 is just too long?

24 MR. NICOLICH: Yes, it's too long. They  
25 make an argument that, well, a prolonged period

1 should be allowed because this is a curative statute.  
2 This is not a curative statute.

3 JUDGE STEIN: What is your proof that  
4 before Mintz and Baum, the - - - the practice was  
5 different? How have you met that burden?

6 MR. NICOLICH: Well, in two ways. Number  
7 one, clear application of the federal law, federal  
8 regulations, and the fact that state law incorporates  
9 them.

10 But as Your Honor pointed out earlier, page  
11 154 of the record, this is part of the PowerPoint  
12 presentation. This is their own evidence. "A  
13 nonresident shareholder is taxed on the pass-through  
14 of the gain from the deemed sale of the assets, but  
15 only to the extent the gain is derived from New York  
16 sources. The gain would not be included in the  
17 numerator of the New York source fraction unless the  
18 nonresident shareholder's stock in the corporation is  
19 employed in another trade or business carried on in  
20 New York State by the shareholder." This is the New  
21 York State Tax Department's own document. So they  
22 have no evidence that shareholders in this situation  
23 were being taxed before this.

24 JUDGE RIVERA: What about Haskell?

25 MR. NICOLICH: And if they were - - -

1                   JUDGE RIVERA: What about Haskell and - - -  
2 well, depending on how you - - - what about - - -

3                   MR. NICOLICH: Haskell - - - if I can just  
4 find it a second. Page 164 of the record; this is  
5 Haskell: "Note when a resident or nonresident  
6 shareholder actually disposes of the shareholder's  
7 stock, any gain on the actual sale of the stock is  
8 not recognized by the shareholder for federal or New  
9 York State personal income tax purposes." This is  
10 under a 338 - - - a deemed liquidation, which is what  
11 we're talking about. Deemed liquidation is what  
12 happened under the federal law and - - - and federal  
13 regulations.

14                   JUDGE ABDUS-SALAAM: But is there any  
15 difference - - - I'll go back to my earlier question  
16 about - - - is there any distinction that this is an  
17 installment sale because it's treated under a  
18 different section of the IRS Code?

19                   MR. NICOLICH: Well -- but the IRS regs,  
20 they treat 338 transactions, which is what this is,  
21 specifically addresses installment sales and says  
22 that a payment under an installment sale is a payment  
23 for the sale of stocks. So those provisions work  
24 together.

25                   I don't know if I've answered your

1 question, but - - -

2 CHIEF JUDGE LIPPMAN: Okay, counselor.

3 Anything else, counselor?

4 MR. NICOLICH: No. If you have no more

5 further questions for me - - -

6 CHIEF JUDGE LIPPMAN: Thank you, counselor.

7 Counselor, rebuttal?

8 JUDGE READ: It is true we've never proved  
9 anything as long as three-and-a-half years before,  
10 have we?

11 MS. VALE: No, that's not true. There are  
12 plenty of cases where it stretches back longer than  
13 three years if you have a curative or clarifying  
14 amendment. In Varrington, it was longer than three  
15 years. In Canisius College, it was longer than three  
16 years. The duration is not a free-floating factor  
17 where you just pick a number and say it's enough or  
18 it's not enough. That doesn't make sense. You have  
19 to look at why you need that duration.

20 JUDGE READ: So this goes back to the  
21 public purpose argument that you made before?

22 MS. VALE: Yes, it all gets tied together.  
23 The curative and clarifying nature of this amendment  
24 affects all of the due process factors. And you  
25 needed the three years because that's how long the

1 tax years stay open. And so if you picked a random  
2 number, if you picked one-and-a-half years, then for  
3 the other one-and-a-half years, you'd still have the  
4 chaos from Baum and Mintz, you'd still have  
5 purchasers not knowing what they're supposed to do  
6 with the asset-sale benefits that they already took,  
7 how they're supposed to keep track of different  
8 valued assets under federal and New York systems, and  
9 you'd still have unintended refunds flowing for that  
10 time period.

11 And I want to stress, what plaintiffs are  
12 trying to say is that a guess at what might be a  
13 reading, in order to get total tax immunity, is  
14 somehow a settled, reasonable expectation that gives  
15 them a due process right.

16 JUDGE ABDUS-SALAAM: But they're saying  
17 this is more than a guess. They're saying they  
18 looked at the way the feds treated this, and there's  
19 supposed to be federal-state conformity, so they  
20 relied on what the feds do in assuming, essentially,  
21 that New York would treat it the same. So what's  
22 your response to that?

23 MS. VALE: We don't think that's the most  
24 reasonable reading of federal law, because they are  
25 ignoring 453B, and even example 10 points to 453B and

1 to 1366 and says you have to look to the pass-through  
2 rules, and that is a very important piece of the  
3 federal treatment.

4 JUDGE READ: So you're saying the federal  
5 law is ambiguous?

6 MS. VALE: Yes, and - - - I mean, we don't  
7 think it's ambiguous; we think the reasonable reading  
8 was our way, but at most, they have identified an  
9 ambiguity, what might be a disconnect between the  
10 federal system and the New York system, and that  
11 doesn't create a reasonable, settled expectation,  
12 back in 2007, to tax immunity. And the deemed  
13 asset-sale part of this transaction is key; it's the  
14 heart of the transaction. It is not just a  
15 liquidation. And what plaintiffs are saying is that  
16 that delay, that one-day or one-month delay, would  
17 make all the difference in the world. It would mean  
18 that all of the deemed asset-sale gain gets  
19 transformed into stock-sale gain and is not taxable.

20 JUDGE RIVERA: But the deemed - - - well,  
21 I'm sorry. But the deemed asset doesn't occur - - -  
22 this fiction doesn't occur without the liquidation,  
23 no?

24 MS. VALE: There is always - - -

25 JUDGE RIVERA: It's part and parcel; you

1 can't do one without the other, correct?

2 MS. VALE: But there's always a deemed  
3 asset sale and there's always a liquidation - - -

4 JUDGE RIVERA: Liquidation.

5 MS. VALE: - - - whether you have an  
6 installment sale or not, and so under plaintiff's  
7 theory, people like the Burtons, who didn't delay  
8 their payments, would have to pay the taxes; the  
9 deemed asset sale would pass through and they would  
10 have to pay. But the Caprios wouldn't, because they  
11 delayed payment by one month. We don't think that's  
12 the way to read federal law. We don't think that's  
13 the way New York ever treated these transactions,  
14 which is clear from the record. And it wouldn't make  
15 sense to do it that way. Why would New York give out  
16 the asset-sale benefits but not collect the  
17 asset-sale taxes?

18 JUDGE RIVERA: I mean, what's the point - -  
19 -

20 MS. VALE: That doesn't make sense.

21 JUDGE RIVERA: What's the point of the  
22 regulation he's referring to?

23 MS. VALE: Of?

24 JUDGE RIVERA: What's the point of that  
25 federal regulation?

1 MS. VALE: To have the liquidation? I  
2 mean, it's the - - - there's a bunch of different  
3 mechanical steps that happen in order to make this  
4 tax fiction, with very real consequences, work. And  
5 part of the process is that they do the liquidation.  
6 But that shouldn't make all of the deemed asset-sale  
7 gains, that were calculated in this case, just vanish  
8 into thin air. That's not fair to other taxpayers  
9 who would still have to pay the taxes under  
10 plaintiff's theory, and it's not fair to purchasers,  
11 who would get thrown into limbo about whether they  
12 should get to keep the benefits if now nobody's  
13 paying the taxes.

14 CHIEF JUDGE LIPPMAN: Okay, counselor,  
15 thanks.

16 MS. VALE: Thank you.

17 CHIEF JUDGE LIPPMAN: Thank you both.  
18 Appreciate it.

19 (Court is adjourned)

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C E R T I F I C A T I O N

I, Sharona Shapiro, certify that the foregoing transcript of proceedings in the Court of Appeals of Caprio v. New York State Department of Taxation and Finance, et al., No. 116, was prepared using the required transcription equipment and is a true and accurate record of the proceedings.

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