

STATE OF NEW YORK  
TAX APPEALS TRIBUNAL

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In the Matter of the Petition :  
of :  
**STRATHMORE BAGELS, INC.** :  
for Redetermination of a Deficiency or for Refund of :  
Corporation Franchise Tax under Article 9-A of the :  
Tax Law for the Years 1984 and 1985. :

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DECISION  
DTA Nos. 809142  
and 809143

In the Matter of the Petition :  
of :  
**STRATHMORE STABLES, INC.** :  
for Redetermination of a Deficiency or for Refund of :  
Corporation Franchise Tax under Article 9-A of the :  
Tax Law for the Years 1981 through 1985. :

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Petitioners Strathmore Bagels, Inc. and Strathmore Stables, Inc., c/o Jerry Steuerman, 6696 Willowood Drive, Boca Raton, Florida 33434, filed an exception to the determination of the Administrative Law Judge issued on November 10, 1993. Petitioners appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Vera Johnson, Esq., of counsel).

Petitioners filed a brief. The Division of Taxation submitted a letter stating it would not be filing a brief. This letter was received on March 8, 1994 which began the six-month period for the issuance of this decision. Oral argument was not requested.

Commissioner Koenig delivered the decision of the Tax Appeals Tribunal. Commissioner Dugan concurs.

**ISSUES**

I. Whether petitioner Strathmore Bagels, Inc. proved entitlement to certain deductions as ordinary and necessary business expenses.

II. Whether petitioner Strathmore Stables, Inc. was the nontaxable corporate-agent for its taxable principal, the sole officer and shareholder.

**FINDINGS OF FACT**

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

**Strathmore Bagels, Inc.**

Petitioner Strathmore Bagels, Inc. was a corporation engaged in the business of wholesaling and retailing bagels in the metropolitan commuter transportation district.

Petitioner Strathmore Bagels, Inc. filed its 1984 and 1985 metropolitan transportation business tax surcharge reports (CT-3M/4M) and its 1984 and 1985 corporation franchise tax reports on March 18, 1985 and March 17, 1986, respectively. Jerry Steuerman signed, as president of petitioner, a consent extending the period of limitation of the assessment of taxes for the audited period until April 15, 1989.

The Division of Taxation ("Division") conducted a franchise tax audit of petitioner's 1984 and 1985 corporation franchise tax reports and metropolitan transportation business tax surcharge reports.

By letter dated January 28, 1987, the auditor requested petitioner's books and records for 1984 and 1985. In response, petitioner Strathmore Bagels, Inc. provided a general ledger, Federal returns and some expense documentation but was unable to provide documentation substantiating the following business expenses that were claimed as deductions on the 1984 and 1985 corporation franchise tax reports:

	<u>1984</u>	<u>1985</u>
automobile expenses	\$ 6,614.00	\$ 3,455.00
equipment rental expenses	18,242.00	2,190.00
insurance expense	<u>6,913.00</u>	<u>6,409.00</u>
TOTAL	\$31,769.00	\$12,054.00

The Division disallowed the above expenses because they were not substantiated but only to the extent of 50% because it attributed the disallowed portion of the reported expenses to the

personal use of petitioner's sole stockholder and officer. The Division also disallowed, as unsubstantiated, a \$1,599.00 auto depreciation expense for the year 1985. Accordingly, the Division calculated the total franchise tax liability for 1984 and 1985 as \$2,126.40 and 1,780.40, respectively, and subtracted the tax reported for those years (\$538.00 for 1984 and \$250.00 for 1985) in determining franchise tax due in the amount of \$1,588.40 for 1984 and \$1,530.40 for 1985. Based on the disallowed expenses, the Division calculated a surcharge tax liability of \$361.49 for 1984 and \$302.67 for 1985 and subtracted petitioner's reported surcharge tax deficiency (\$91.00 for 1984 and \$43.00 for 1985) to arrive at a surcharge deficiency of \$270.49 for 1984 and \$259.67 for 1985.

The Division issued to petitioner Strathmore Bagels, Inc. four notices of deficiency, dated January 23, 1989, as follows:

<u>Notice Number</u>	<u>Period</u>	<u>Type of Tax</u>	<u>Amount</u>
C890123775F	1984	corporation franchise tax	\$1,588.40
C890123776S	1984	surcharge	270.49
C890123777F	1985	corporation franchise tax	1,530.40
C890123778S	1985	surcharge	259.67

These notices also included penalties and interest in addition to the above-stated amounts.

A conciliation conference was held on August 8, 1990. By Conciliation Order dated November 23, 1990, the conferee sustained the four statutory notices.

Petitioner Strathmore Bagels, Inc. filed a petition, dated January 18, 1990, claiming that the Division erred by improperly denying deductions for an automobile expense, equipment rental, insurance premiums and automobile depreciation. Petitioner alleged that all of those deductions consisted of items that were paid or incurred by it as ordinary and necessary expenses of its trade or business and, thus, qualify as deductions under sections 162 and 168 of the Internal Revenue Code of 1954, as amended.

The Division filed an answer, dated March 6, 1991, affirmatively stating, inter alia, that petitioner has the burden of proving that deficiencies are erroneous pursuant to Tax Law § 1089(e).

Strathmore Stables, Inc.

Petitioner Strathmore Stables, Inc. is a New York corporation which was incorporated on September 21, 1981 and was owned by shareholders Jerry and Elaine Steuerman. Strathmore Stables, Inc.'s principal business activity was horse racing.

The Division conducted a personal income tax audit of petitioner's shareholders, Jerry and Elaine Steuerman, in which the Division disallowed Schedule C losses reported by the Steuermans on their personal income tax returns. The Division disallowed a reported net loss of \$78,768.00 for 1984 and a net loss of \$107,764.00 for 1985 because the business activity resulting in the losses was petitioner's business activity. The Steuermans had not filed a petition for Subchapter S treatment.

According to an affidavit by the Division's auditor, Lawrence Wolff, petitioner Strathmore Stables, Inc. not only filed a certificate of incorporation on September 21, 1981, it also conducted business as a corporation, maintained corporate checking accounts, and received income and incurred debt in its own name.

As a result of the Steuerman audit, the Division commenced an audit of petitioner Strathmore Stables, Inc. and discovered that petitioner never filed a corporation franchise tax return or surcharge report for the years 1981 through 1985. The Division computed petitioner's corporation tax liability for 1984 and 1985 by utilizing the amounts reported in the Steuermans' Schedule C which reflected gross receipts of \$136,299.00 in 1984 and \$136,173.00 for 1985. To these amounts, the Division added additional receipts of \$42,986.00 for 1984 and \$239,039.00 for 1985 based on its analysis of petitioner's cash payouts and bank deposits. From the total receipts for 1984 and 1985, the Division subtracted the cost of goods sold and other expenses for the respective years. Also, for 1984 the Division subtracted the supplemental loss reported by the Steuermans as reflected in their 1984 Schedule C and added supplemental gain reported on

their 1985 Schedule C. The Division calculated that petitioner Strathmore Stables should have reported income in the amount of \$58,882.00 for 1984 and \$138,625.00 for 1985. Based on this income, the Division determined a minimum corporate tax due of \$250.00 for 1981 through 1984 and \$13,625.00 for 1985.

The Division also used its estimation of income to calculate Metropolitan Transportation Business Tax ("MTBT") surcharge for the years 1982 through 1985. Because the MTBT surcharge was not effective in 1981, the Division did not assess a surcharge for 1981.

The Division issued to petitioner Strathmore Stables, Inc., nine notices of deficiency, dated May 2, 1989, as follows:

<u>Notice Number</u>	<u>Period</u>	<u>Type of Tax</u>	<u>Amount</u>
C890502775F	12/31/81	corporation franchise tax	\$ 250.00
C890502776F	12/31/82	corporation franchise tax	250.00
C890520777S	12/31/82	surcharge	45.00
C890520778F	12/31/83	corporation franchise tax	250.00
C890520779S	12/31/83	surcharge	43.00
C890520780F	12/31/84	corporation franchise tax	250.00
C890520781S	12/31/84	surcharge	42.50
C890502782F	12/31/85	corporation franchise tax	13,862.50
C890502783S	12/31/85	surcharge	2,356.63

The nine notices also contained additional amounts for penalties and interest.

A conciliation conference was held on August 8, 1990. The conferee, by Conciliation Order dated October 26, 1990, sustained the nine statutory notices.

By petition dated January 18, 1991, petitioner challenged the nine statutory notices of deficiency. In this petition, petitioner Strathmore Stables, Inc. contended that the Division erred in issuing the notices based on the following allegations:

"The Commissioner has erred by incorrectly assigning to the taxpayer, income and expenses properly attributable to the taxpayer's sole officer and shareholder under Section 61 regulations thereunder, and applicable case law (see eg., Comm. v. Bollinger, Jr., et al., 88-1 USTC 9233). Specifically, the Commissioner has refused to recognize the taxpayer's status as agent rather than principal with respect to all transactions alleged against it for the ownership and maintenance of race horses."

The Division filed an answer dated March 15, 1991 stating, inter alia, that the Division estimated petitioner's franchise tax liability pursuant to Tax Law § 1081(a) based on records made available by petitioner such as purchase invoices, expense documentation and checking account; and that pursuant to Tax Law § 1089(e), petitioner has the burden of proving that the Division's estimations are erroneous.

***OPINION***

In the determination below, relating to Strathmore Bagels, Inc., the Administrative Law Judge held that "the record does not indicate that petitioner provided any substantiation to support either the amount of the deduction or entitlement to the deductions as ordinary and necessary business expenses" and, further, "as no evidence has been introduced to substantiate petitioner's allegation in its petition that the deductions related to ordinary and necessary business expenses, it has not carried its burden of establishing entitlement to the deductions" (Determination, conclusion of law "B").

In her determination relating to Strathmore Stables, Inc., the Administrative Law Judge held that when a corporation's income is not accurately reflected in its books and records, the Division may use an indirect method, "cash availability" analysis to determine deficiencies in the corporation franchise tax and the taxpayer then has the burden of proving by clear and convincing evidence that the method used to arrive at the franchise tax deficiencies was erroneous.

The Administrative Law Judge also held that while petitioner Strathmore Stables, Inc. argues it is a nontaxable agent of its principal, the sole officer and shareholder, and the income and expenses are, therefore, attributable to the principal only, "petitioner submitted no evidence to support the genuineness of the agency relationship" and absent such evidence, "petitioner has not carried its burden of proving that the Division's audit results were erroneous" (Determination, conclusion of law "C").

On exception, petitioners, by Jerry Steuerman, ask for help in resolving this matter and state that since the beginning of 1990 they have tried to compensate everybody involved but in August of that year Mr. Steuerman lost his business due to being totally disabled. Further, Mr. Steuerman points out that he is living on Social Security Disability having no income, no money and is barely sustaining himself.

The Division did not submit a reply brief.

We affirm the determination of the Administrative Law Judge.

In addition, because we find that the Administrative Law Judge completely and adequately addressed the issues before her, we see no reason to analyze these issues further; nor do we see any reason to hold otherwise and, therefore, affirm the Administrative Law Judge based on her determination.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of petitioners Strathmore Bagels, Inc. and Strathmore Stables, Inc. is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petitions of Strathmore Bagels, Inc. and Strathmore Stables, Inc. are denied;
4. The four notices of deficiency dated January 23, 1989 issued to Strathmore Bagels, Inc. are sustained; and
5. The nine notices of deficiency dated May 2, 1989 issued to Strathmore Stables, Inc. are sustained.

DATED: Troy, New York  
August 25, 1994

/s/John P. Dugan  
John P. Dugan  
President

/s/Francis R. Koenig  
Francis R. Koenig  
Commissioner