STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
SOL DREBIN	:	DECISION DTA No. 812784
for Redetermination of a Deficiency or for Refund of New York State and New York City Income Taxes under Article 22 of the Tax Law and the New York City Administrative Code for the Years 1982 through 1987.	:	

Petitioner Sol Drebin, 1655 43rd Street, Brooklyn, New York 11204, filed an exception to the determination of the Administrative Law Judge issued on February 29, 1996. Petitioner appeared by Morris Werner, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Kenneth J. Schultz, Esq., of counsel).

Petitioner filed a brief in support of his exception. The Division of Taxation did not file a brief. Petitioner's request for oral argument was denied.

Commissioner Jenkins delivered the decision of the Tax Appeals Tribunal. Commissioner DeWitt concurs. Commissioner Pinto took no part in the consideration of this decision.

ISSUES

I. Whether petitioner has proven by clear and convincing evidence that the Division of Taxation erred in determining that he owed additional New York State and New York City personal income tax attributable to constructive dividends and/or additional unreported salary or other income received from Intercity Electrical Contracting Corp. and/or Century Electrical Contracting Corp.

II. Whether the Division of Taxation is prohibited by the period of limitations on assessment of additional taxes pursuant to Tax Law § 683 from issuing assessments for the years 1982, 1983 and 1984.

III. Whether petitioner has demonstrated that his underpayment of New York State and New York City personal income taxes was attributable to reasonable cause and not willful neglect such that the penalties asserted pursuant to Tax Law § 685(p) for the years 1985, 1986 and 1987 should be abated.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "1," "2," "5," "6," "7," "8," "11," "12," "15" and "18" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

We modify finding of fact "1" of the Administrative Law Judge's determination to read as follows:

> Petitioner, Sol Drebin (also known as Label Drebin), was a principal, officer and sole shareholder in a company known as Intercity Electrical Contracting Corp. ("Intercity") during the years in issue, 1982 through 1987 (Exhibit "J"). During this same period he was also principal, officer and owner of Century Electrical Contracting Corp. ("Century").
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> The business operations of Century were merged into the business operations of Intercity in 1982 or 1983. While these corporations may have had separate corporate identities, their business operations, by and through Sol Drebin, became so intertwined, based on the facts in this record, that they functioned as a single entity under the name of Intercity and their separate corporate identities were, as best, illusory.
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> The offices of Century and Intercity were maintained at the residence of Sol Drebin at 1655 43rd Street, Brooklyn, New York.
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> Century had a second office maintained at 131 Rutledge Street, Brooklyn, New York out of which Carl Weiss purportedly could perform contract work for Century. Each office kept its own set of books and records and retained its own profits (Exhibit "G").
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> There is no evidence in this record that Carl Weiss ever performed any contract work or generated any receipts or profits during the audit period for Century. There is also no evidence that petitioner, Intercity or Century paid Weiss any monies for contract services performed and/or as profits earned.
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> During the audit period, Sol Drebin was, at various unspecified

> times, president, vice president and/or treasurer of Intercity. His son, Joseph Drebin, also held one or more offices at various times, again unspecified.[1]

We modify finding of fact "2" of the Administrative Law Judge's determination to read as follows:

> Sometime prior to December 1988, a Superior Court Information was issued against Century, Intercity, and Joseph Drebin, as officer, alleging that they had, with intent to evade payment of corporate income taxes, failed to file corporate income tax returns.
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> Counts one and three charged that Intercity and Century committed the crime of repeated failure to file utility tax or corporate taxes in violation of section 11-4003 of the Administrative Code of the City of New York. Specifically, these counts charged that Intercity and Century willfully failed to file corporate income tax returns for Intercity for 1984, 1985 and 1986 and failed to file corporate income tax returns for Century for 1983, 1984 and 1985. Both corporations had unpaid tax liabilities for each of those years.
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> Counts two and four charged that Intercity and Century committed the crime of repeated failure to file corporate franchise tax returns in violation of section 1803 of the New York State Tax Law. Specifically, these counts charged that Intercity and Century, with intent to evade payment of franchise tax imposed by Article 9-A of the State Tax Law, willfully failed to file corporate income tax returns for taxable years 1984, 1985 and 1986 with respect to Intercity and failed to file corporate income tax returns for taxable years 1983, 1984 and 1985 with respect to Century. Both of these corporations had unpaid tax liabilities in excess of $250.00 with respect to each of these consecutive taxable years.
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> All four counts of the Superior Court Information were Class E felonies.[2]

In a letter from Assistant District Attorney Roslynn Mundell to the defendants' attorney, Jacob Laufer, dated December 19, 1988, the terms of a plea agreement between the District

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[1] We modified finding of fact "1" of the Administrative Law Judge's determination to more clearly reflect the record.

[2] We modified finding of fact "2" of the Administrative Law Judge's determination to more fully set forth facts in the record.

Attorney and the defendants were setforth in detail. The defendants included Intercity, Century, Label Drebin (petitioner herein) and Joseph Drebin, his son. The calendar years covered by the plea agreement were 1982 through 1987. Both Century and Intercity agreed to be prosecuted in accordance with the Superior Court information and pled guilty to one count of repeated failure to file corporate taxes, in violation of Tax Law § 1803, an E felony, and one count of repeated failure to file utility tax or corporate taxes, in violation of section 11-4003 of the New York City Administrative Code.

The corporate taxes determined to be due from the two corporations for the years 1982 through 1987 were based upon combined earnings for both corporations reached in an agreement between the District Attorney's office and the representatives of the defendants, to wit: Max Wasser, CPA and Jacob Laufer, Esq. The combined earnings and tax thereon for the two corporations for the years in issue were determined to be as follows:

	Gross Receipts	Net Profit	NYS Tax	NYC Tax
1982	$ 85,132	$ 21,283	$ 2,124	$ 1,911
1983	811,238	202,809	20,281	18,253
1984	1,252,276	313,069	31,307	28,176
1985	990,523	247,631	24,763	22,287
1986	746,654	186,663	18,666	16,800
1987	849,252	212,313	21,231	19,198

These figures appear in the record in a letter from Mr. Laufer to Mr. Wasser, dated December 29, 1988.

In a letter from Roslynn R. Mundell, Assistant District Attorney, to Assistant Commissioner Bruce Kato of the New York City Department of Finance, dated January 13, 1989, Ms. Mundell described how the amounts of tax were calculated. She explained that the amount of tax was calculated on a net profit figure established by deducting 75% from the amount of gross income as the cost of goods sold. This deduction was based on standards established by Dun and Bradstreet for the cost of doing business for this type of company operating in the New York City area. Three methods of calculating gross income were compared by the District Attorney's office, to wit: bank deposits were included as gross

income; "FISA" records showing all payments to both corporations on City contracts; and gross income figures submitted by petitioner's accountant, Max Wasser. Since the figures submitted by the accountant, Max Wasser, were reasonable in comparison to the amounts arrived at using the other methods, they were accepted.

Petitioner submitted a two-page chart from a publication named "Investor's Monthly", dated March 1995, which showed the pay-out ratio for major corporations, i.e., the annual dividend expressed as a percentage of estimated earnings.

We modify finding of fact "5" of the Administrative Law Judge's determination to read as follows:

> In conducting his contracting business, petitioner was not authorized to legally get contracts for New York City electrical jobs, and needed to align himself by agreement with a properly licensed contractor in order to secure New York City contracts. An agreement for that purpose, dated October 30, 1981, between Century, Carl Weiss and petitioner, was executed shortly before Intercity assumed the business operations of Century. However, as noted earlier, there is no credible evidence that Carl Weiss ever did anything more under this agreement than to provide the "cover" of his license. There is no credible evidence that Weiss performed any contract work under Century's name or that petitioner had agreements to share any profits with Weiss or any other contractor during the years in issue or if profits were shared.[3]

We modify finding of fact "6" of the Administrative Law Judge's determination to read as follows:

> On December 22, 1988, Joseph Drebin, on behalf of himself and the boards of directors of the two corporations, executed waivers of indictment, indicating acceptance of the plea agreement.
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> On January 4, 1989, the defendants, Intercity and Century, appeared by Joseph Drebin for pleas and sentencing before the Honorable John A. K. Bradley, Justice of the Supreme Court, and entered their pleas as described above. In addition, Intercity, by its vice president, Joseph Drebin, executed two affidavits confessing judgment ("confessions of judgment") to the amounts admitted to be

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[3] We modified finding of fact "5" of the Administrative Law Judge's determination to more completely set forth the facts in the record.

due and owing to the State and City of New York in the sums of $118,372.00 and $106,625.00, respectively.

Upon the defendants being arraigned for sentencing, the Court, in order to determine the amount of the fine, inquired of Assistant District Attorney Mundell as to the amount of the criminal gain involved in this case. Ms. Mundell responded, in part:

> "the amount of the gain in this case is at a minimum $225,000.00, which represents the amount of unpaid tax for the period 1982 through 1987" (Division's Exhibit "F," sentencing transcript, p. 5).

At this, Jacob Laufer, attorney for all of the defendants, stated:

> "[w]e specifically agree with Miss Mundell's recounting to the Court of the tax that should have been paid and not paid, your Honor" (Exhibit "F," sentencing transcript, pp. 5-6).

The Court then asked Mr. Drebin if he agreed with what Mr. Laufer had said. Mr. Drebin said, "Yes."[4]

We modify finding of fact "8" of the Administrative Law Judge's determination to read as follows:

A memorandum from Paul Giskin, Associate Fraud Investigator with the New York City Department of Finance, dated March 2, 1989, reported some of the details of the investigation performed with regard to Century, Intercity, petitioner and Joseph Drebin. He stated that information obtained from the New York City Department of Housing, Preservation and Development ("HPD") indicated that the two companies received in excess of $3,400,000.00 between 1983 and 1987 in contract work performed for HPD.

During this period, neither corporation filed any corporation tax returns. Despite numerous attempts to contact the principals of the corporations, Carl Weiss of Century and Label Drebin of Intercity, including subpoenas for tax returns, workpapers, etc., these individuals were uncooperative and no documents were produced. Given the evidence of tax fraud, the case was referred to the Manhattan District

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[4] We modified finding of fact "6" of the Administrative Law Judge's determination to more completely set forth the facts in the record. The substance of the Administrative Law Judge's finding of fact "7" has been incorporated into this modified finding.

Attorney's office for criminal prosecution.[5]

Both confessions of judgment executed by Joseph Drebin stated that the confessions were made without prejudice to claims by both the New York State Department of Taxation and Finance and the New York City Department of Finance for accrued interest and/or civil penalties.

The Division sent an appointment letter to petitioner on November 21, 1989, which requested documents pertaining to petitioner's personal income tax returns for the years 1986 and 1987. The letter also enclosed a power of attorney form in case petitioner chose to appear by a representative.

In fact, in response to this letter, Mr. Max Wasser called the auditor on December 4, 1989 to reschedule the appointment and to say that he would be forwarding a power of attorney. The power was presented to the Division by Mr. Wasser on January 4, 1990.

We modify finding of fact "11" of the Administrative Law Judge's determination to read as follows:

> The Division assumed that the excess unreported income of the corporations was distributed to the Drebins as constructive dividends or excess wages ("unreported income"), since it was never provided with any corporate records or other evidence of how the excess unreported income from Century and Intercity was disposed. However, an entry in the auditor's log, dated March 2, 1990, indicated that Mr. Wasser told her that the unreported income was given to charity. The auditor asked for confirmation of this fact on March 2 and April 6, 1990, and also in a letter to Mr. Wasser, dated April 6, 1990. While Mr. Wasser promised to provide the documentation "within a couple of weeks," no evidence of such charitable contributions was produced. This claim that the money was given to charity is now disavowed by petitioner as mere hearsay.
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> No business records for Century or Intercity were ever provided to the criminal investigators or to the Division's auditor. No evidence accounting for the unreported corporate income has ever been provided. No corporate records have ever been produced to rebut the

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[5] We modified finding of fact "8" of the Administrative Law Judge's determination to more fully reflect the facts in the record.

Division's claim that petitioner is principal owner and officer of both corporations.[6]

We modify finding of fact "12" of the Administrative Law Judge's determination to read as follows:

> At the hearing in this matter, petitioner's attorney expressly stated that petitioner was not raising the issue of the statute of limitations (tr., p. 68). Petitioner, at hearing, submitted the "Business Entity Questionnaire" for qualification as a bidder, proposer and subcontractor, dated November 25, 1987, submitted by Intercity to the HPD, which indicated that the principals in the corporation were Label Drebin, Joseph Drebin and Ivon Coleman. It stated that Sol and Joseph Drebin each owned 40% of the stock (as of the end of 1987). Petitioner's son, Joseph Drebin, signed the application as vice president.
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> It is noted that this "Business Entity Questionnaire" contained apparently intentional misstatements of fact. Question "5.c." asked if any of the corporation's officers, directors or employees were affiliated with the lessor/owner of the property being used by the corporation, and the answer given was "No" even though Sol Drebin was listed as the lessor/owner of the property.
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> Question "6.a." asked for the principals in the business and Ivon Coleman was listed as a 20% owner and president, even though petitioner testified that he and his son were the only officers and never mentioned another owner.
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> Question "8.b." asked if Intercity had done business with the City of New York during the past five years. The answer given was "No." To question "13," which asked if the submitting business entity (Intercity) had filed all Federal, State and New York City tax returns for the past three tax years, the answer given was "Yes."
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> There is no evidence in the record indicating how, or if, the profits of the business were divided. In fact, the only credible evidence in the record relates to petitioner's, and his son's, use of Intercity and Century in generating income from HPD. There is no evidence that any other person, e.g., Carl Weiss, provided contractual services or generated income for Century or Intercity after the 1981 agreement was executed by petitioner and Weiss. There is no credible evidence that Ivon Coleman had any role with either of these two corporations or their business activities during the audit period. Carl Weiss and

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[6] We modified finding of fact "11" of the Administrative Law Judge's determination to more fully reflect the facts in the record.

Ivon Coleman both remain "names on a page."[7]

Petitioner was not able to recall when it was that Intercity assumed the business operations of Century, but, as stated above, believed it was in 1982 or 1983. No documentary evidence of this was produced even though the Division requested it. Even the agreement between petitioner, Century and Mr. Carl Weiss, entered into on October 30, 1981, did not establish that Century had any independent business operations during the audit period.

Petitioner thought about closing down his contracting business in 1982, but remained in business until 1987 or 1988, when he turned it over to his son, Joseph. Petitioner was ill during some of the audit period and allowed his son to handle the business during these unspecified periods.

We modify finding of fact "15" of the Administrative Law Judge's determination to read as follows:

> During most of the audit period, petitioner drew a salary from Intercity. Petitioner filed a State personal income tax return for 1982 which reported gross income of $18,617.00. Petitioner's State personal income tax returns for 1985, 1986 and 1987 report income from Intercity, but no income is reported as having been received from Century. This would appear consistent with the finding that Intercity was the only active corporation.
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> The offices of Intercity and Century were in petitioner's two-family home and the corporations received their mail and check payments from New York City's HPD projects there. Petitioner admitted that both he and his son, Joseph, opened the mail and deposited the checks received from the New York City projects. Both petitioner and his son had the authority to sign checks for Intercity.
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> Petitioner's testimony at hearing regarding the operations of his corporations was vague at best. Petitioner did not recall what office he held in Intercity, but acknowledged he was an officer. He did not remember if he was a director of Intercity.
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> When it came to taxes, whether City, State or Federal, he

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[7] We modified finding of fact "12" of the Administrative Law Judge's determination to more fully set forth the facts in the record.

> realized they existed and had to be paid, but little else. He admitted to no role in assisting in the preparation of returns. He left that sort of thing up to his accountant or bookkeeper; at other points in his testimony, it was his son's responsibility (tr., pp. 45-46). Although Intercity and Century were his corporations, he claims he did not get involved with which taxes had to be paid, how the returns were prepared or how much tax was due. Petitioner's testimony was not credible.
>
> At hearing, petitioner brought no corporate books or business records for Intercity or Century to substantiate his claims as to the manner in which business was conducted by Intercity or Century.[8]

Petitioner's gross income for each of the years 1982 through and including 1987 was increased by the net profit figure calculated by the District Attorney's office, as set forth above, and petitioner's taxable income was adjusted accordingly and the New York State and New York City tax liabilities recomputed. A Statement of Personal Income Tax Audit Changes for the years 1982 through 1987, dated September 12, 1990, was issued to petitioner and his spouse (who did not file a petition herein), setting forth in detail the additional tax, penalties and interest due.

Like this forum, the auditor was provided with absolutely no credible evidence of ownership. In the audit report, the auditor stated:

> "1. [Label] Drebin, as well as Joseph Drebin, are held individually responsible as corporate officers for the full amounts of the unreported income computed for each year, 1982-1987.
>
> "2. It is to be noted that this auditor has taken an inconsistent position by assessing both Label Drebin and Joseph Drebin [Audit # D-6364] for the additional tax and related penalties and interest on the unreported income for 1982-1987. In the event that either is found to be fully liable for the assessment, no liability will exist against the other."

The Division issued a Notice of Deficiency to Sol and Bayle Drebin, dated February 15, 1991, which asserted additional tax, penalty and interest in the sum of $439,393.91 for the years

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[8] We modified finding of fact "15" of the Administrative Law Judge's determination to more completely reflect the record.

1982 through 1987. The Division asserted fraud penalty pursuant to Tax Law § 685(e)(1); additional penalty due to fraud pursuant to Tax Law § 685(e)(2); and penalty for substantial understatement of liability pursuant to Tax Law § 685(p).

We modify finding of fact "18" of the Administrative Law Judge's determination to read as follows:

> Petitioner filed an application for a conference in the Bureau of Conciliation and Mediation Services which was held on November 24, 1993. An Order was issued on April 8, 1994, which sustained the tax deficiency in its entirety but modified the penalties asserted by permitting the assessment of Tax Law § 685(p) penalty for only the years 1985, 1986 and 1987. Fraud penalties were canceled, and there is no indication in the record as to the conferee's decision in this regard.[9]

OPINION

The Administrative Law Judge held that petitioner had failed to carry his burden of proof to show: (i) that the District Attorney's office erred in utilizing the Dun and Bradstreet index for purposes of calculating the additional taxes due from Century and Intercity; (ii) that the District Attorney's figures were inaccurate; or (iii) that the use of the Dun and Bradstreet index lacked a rational basis (Determination, conclusion of law "A").

The Administrative Law Judge also concluded that: (i) petitioner failed to demonstrate that the personal income tax assessment against him was erroneous or lacked a rational basis (Determination, conclusion of law "B"); (ii) failed to show by clear and convincing evidence that either the method used to arrive at the personal income tax assessment, or the assessment itself, was erroneous (Determination, conclusion of law "C"); and (iii) failed to demonstrate reasonable cause for the abatement of penalties (Determination, conclusion of law "E").

The Administrative Law Judge also held that the Division: (i) properly concluded, in the

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[9] We modified finding of fact "18" of the Administrative Law Judge's determination by adding the last sentence to more fully reflect the record.

absence of proof to the contrary, that Sol Drebin benefitted from the excess income to the corporations; (ii) was justified in relying on the District Attorney's finding of excess corporate income; and (iii) properly inferred that such excess income in these closely-held corporations was passed through to its principals/shareholders (Determination, conclusion of law "D").

Petitioner, on exception, challenges all of the Administrative Law Judge's conclusions of law and the facts upon which they are based.

Petitioner argues that the figures used by the District Attorney do not accurately reflect the business of Century and Intercity because the business operations were not like those corporations which form the basis for the Dun and Bradstreet report.

Petitioner questions the net profit figures used by the District Attorney because, he says, they were derived by threat of incarceration to his son, Joseph Drebin. Petitioner claims that the Dun and Bradstreet revenue figures cannot be applied to the instant matters because of the neighborhoods in which the work was done, the scene of alleged rampant pilferage, and the fact that, as a result of vandalism, jobs had to be repeated at no charge.

Petitioner also contends that the Division lacked a basis for assuming petitioner was the sole shareholder of both corporations and that he received actually or constructively any of the earnings of the corporations as constructive or actual dividends.

Petitioner argues that any statement made by his accountant, Max Wasser, concerning the disposition of the net profit of the corporations, i.e., gifts to charity, was hearsay and inadmissible.

Petitioner argues that the Division's assessment has no rational basis and that substantial evidence has not been introduced to sustain the assessment. He argues that the Division did not show, by reasonable inference from the facts, that any income was derived by him from the corporations or how much.

We affirm the determination of the Administrative Law Judge.

Petitioner's liability is derived from the outcome of a criminal investigation of Century, Intercity, petitioner, and his son, Joseph, by the New York County District Attorney. The District Attorney's office determined net profit figures for the companies for the years 1982 through 1987, which were consistent with figures submitted by petitioner's own accountant. These net profit figures were determined to be constructive or actual dividends ("excess income")[10] to petitioner or excess salary, and constitute the basis of the assessment at issue herein.

Petitioner contends that the District Attorney's office erred in its utilization of the Dun and Bradstreet index for purposes of calculating the additional taxes due from Century and Intercity. He makes this contention even though his own accountant provided the gross receipts figures to the District Attorney's office which were adopted and his son, Joseph Drebin, vouched for the accuracy of those figures and the Dun and Bradstreet index in his plea agreement. Petitioner submitted figures from "Investor's Monthly" which purported to show that the numbers used by the District Attorney's office were not accurate, but the figures from "Investor's Monthly" do not address the specific circumstances of Century and Intercity and are, therefore, irrelevant to the circumstances and corporations herein.

Petitioner did not suggest the substitution of a different external index and did not offer any evidence which disputed the District Attorney's findings with respect to the corporations' tax liability. Petitioner owned Intercity and Century and, along with his son, ran these corporations, yet he did not provide books and records of either Century or Intercity which would have established a different tax liability. As the Administrative Law Judge noted, this is a glaring failure of proof. To date, no books and records of either corporation have been submitted into evidence by petitioner. In light of the fact that the corporations' own accountant submitted adjusted gross income figures which confirmed the accuracy of the methods utilized by the District Attorney's office, i.e., bank deposits and proceeds from City contracts, petitioner has

[10]The term "excess income" is used here to refer to personal income in excess of that which was reported by petitioner.

failed to carry his burden of showing that said figures were inaccurate or that the application of the Dun and Bradstreet index lacked a rational basis.

Petitioner has also failed to demonstrate that the personal income tax assessment was erroneous. We have spoken to many of petitioner's arguments in our decision in Matter of R & J Automotive (Tax Appeals Tribunal, June 15, 1989) where we stated:

> "In a sales and use tax audit, resort to external indices as a method of computing sales tax liability must be founded upon a determination of the insufficiency of the taxpayer's record keeping which makes it virtually impossible to verify sales receipts and conduct a complete audit (Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 411 NYS2d 41). This standard, requiring demonstrably inadequate records before an indirect auditing technique may be used, has been explicitly rejected in audits of income for personal income, non-resident earnings and unincorporated business taxes (Matter of Giuliano v. Chu, 135 AD2d 893, 521 NYS2d 883; Matter of Hennekens v. State Tax Commn., 114 AD2d 599, 494 NYS2d 208). The distinction between an income tax audit and a sales tax audit centers on the type of tax being imposed (Hennekens v. State Tax Commn., supra). While sales tax audits seek recovery of taxes imposed directly upon verifiable receipts as evidenced by books and records which are required to be maintained (Matter of Licata v. Chu, 64 NY2d 873, 874, 487 NYS2d 552) audits involving the imposition of tax on income concern the receipt of income which cannot easily be verified by reference to books and records (Matter of Hennekens v. State Tax Commn., supra). The standard articulated by the courts of New York concerning audits of income is that indirect auditing methods are proper where the taxpayer's income is not accurately reflected in his books and records (see, Matter of Giuliano v. Chu, supra; Matter of Hennekens v. State Tax Commn., supra; Matter of Checho v. State Tax Commn., 111 AD2d 470, 488 NYS2d 859)."

Petitioner's arguments that the Division lacked a rational basis for its assessment and that the assessment is not supported by substantial evidence do not recognize the Division's superior right to utilize an indirect auditing method in the case of personal income tax, where receipt of the income cannot easily be verified by reference to books and records (see, Matter of Hennekens v. State Tax Commn., supra).

Application of the R & J Automotive principles to the instant matter supports the audit methodology chosen and utilized by the Division to compute the additional personal income tax

due.

Further, the circumstances of this matter are not sympathetic to petitioner. Petitioner's son and business partner, Joseph Drebin, signed statements for both of petitioner's corporations, as a director of both and a vice president of Intercity, with the authority to bind them to the most grave of consequences, pleading to criminal conduct. Part of the plea agreements provided that petitioner would not be prosecuted by the District Attorney for his role in the failure of Intercity and Century to file City and State corporate tax returns for the calendar years 1982 through 1987.[11] Although petitioner argues that his son only agreed to the terms of the settlement to protect him and that he did so under duress, there is no evidence to support such a bald assertion. It is noted that petitioner benefitted greatly from this plea agreement.[12] Petitioner admitted that he held the office of president and/or vice president of Intercity during the years in issue, received a salary, signed checks, received and deposited payments on City contracted jobs and maintained the offices of the corporation in part of his two-family house. By the confession of judgment signed as part of the plea agreement, Intercity, as the only active corporation, agreed to pay the whole tax liability asserted against it and Century. It is concluded that the reason for Intercity's willingness to assume the liabilities of both corporations is that it, not Century, was the actual operating, revenue-generating corporation. Intercity was petitioner's wholly-owned corporation. All the mail of the corporation was received by the corporation at petitioner's home address, including the checks received in payment for the jobs it did for HPD. Petitioner admitted that the business of Century ceased sometime during the years 1982 or 1983, and that its operations became one with Intercity, consistent with the Division's theory of assessment of petitioner. Indeed, petitioner produced no credible evidence that Century was anything but a shell corporation with a license. Petitioner submitted absolutely no evidence of

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[11]And for his failure to file personal income tax returns for 1983 and 1984.

[12]By not being prosecuted.

the corporate identities, i.e., their books and records or minutes of meetings by the directors, officers or shareholders. Coupled with the lack of documentary evidence concerning Intercity's business operations, petitioner also had a very hazy and incomplete memory of the events which took place during the audit period vis-a-vis the corporations and specific events with respect to his involvement with them. Petitioner never explained his failure to produce his corporate records.

Since petitioner, to this day, has not produced any records to dispute the Division's findings with regard to the additional income to Intercity and Century, there is no basis for disturbing those findings.

The only evidence submitted by petitioner with regard to the issue of the corporate liability and the derivative personal income tax liability was some of the correspondence with respect to the criminal investigation and pleas, the qualification application filed with the City of New York by Intercity in November of 1987, the agreement between Century, Carl Weiss and petitioner in October of 1981 regarding the business relationship between the parties and the dividend analysis of major corporations by "Investor's Monthly" for the month of March 1995.

Buttressing this paucity of proof was the vague and incomplete testimony of petitioner, who could not remember much about the salient details of either Century or Intercity. Such testimony, as noted earlier, was not credible.

Petitioner cites to several cases where courts have discussed the "substantial evidence" rule: Matter of Vogt v. Tully, (53 NY2d 580, 444 NYS2d 441); Matter of Clark v. Bouchard (103 AD2d 899, 478 NYS2d 131); Matter of Williams v. Coughlin (145 AD2d 771, 535 NYS2d 499); Matter of Donahue v. Chu (104 AD2d 523, 479 NYS2d 889); and Matter of Kaskel v. New York State Tax Commn. (111 AD2d 431, 488 NYS2d 322). All of these cases emphasize the need for there to be substantial evidence in the record to support the assessment and that without such evidence the determination will be annulled.

In the instant matter, the Division, through its tax enforcement investigators and later through its auditor, made several requests for information about the business operations of Century and Intercity and the disposition of the excess income, but received no response from petitioner.

Where, as here, a taxpayer fails or refuses to explain the disposition of unreported corporate income, it can properly be deemed a constructive dividend paid to the owners of a closely-held corporation such as Intercity and Century (see, Matter of Petito, Tax Appeals Tribunal, October 17, 1991; Matter of Beagle, State Tax Commn., May 28, 1986).

Here, petitioner provided no documentation or cooperation to the Division to assist in determining what happened to this excess income. Accordingly, the Division utilized reliable information from the District Attorney's office regarding excess income received by two corporations -- closely held by petitioner -- and properly made the logical but rebuttable presumption that the excess net profit had passed through to the shareholders, i.e., petitioner.

The Division's position was supported by the statement of petitioner's own accountant who told the Division's auditor that the excess income was given to charity. This statement supports the Division's conclusion that the unreported corporate income was received by petitioner as a constructive dividend. Petitioner rejects his accountant's statement as "mere hearsay" and inadmissible. Petitioner is correct that the auditor's statement is hearsay. However, hearsay is admissible (People ex rel Vega v. Smith, 66 NY2d 130, 495 NYS2d 332) and may constitute substantial evidence in an administrative proceeding (Matter of Robert OO v. Dowling, 217 AD2d 785, 629 NYS2d 494, affd 87 NY2d 1043, 644 NYS2d 139).

We note that the evidence in the record is sufficient to conclude that the active, revenue-generating corporation for the audit period was Intercity. There is also evidence in the record to support the conclusion that petitioner was the sole shareholder and president of Intercity and we so conclude. As the sole shareholder and president, petitioner was in the best position to produce books and records to show the interaction of Intercity and Century, and show how, and

to whom, the excess income of his corporations was distributed. He did not come forward with such evidence. In the absence of proof to the contrary, it was reasonable for the Division to conclude that the subject unreported income was paid to petitioner as dividends (see, Matter of Petito, supra; Matter of Beagle, supra). We take the strongest possible negative inference from petitioner's failure to present evidence that would show the ownership and officers of Intercity and Century and present books and records of the business operations to show the disposition of the corporations' unreported income (see, Noce v. Kaufman, 2 NY2d 347, 161 NYS2d 1; Milio v. Railway Motor Trucking Co., 257 App Div 640, 15 NYS2d 73) and conclude that petitioner did not produce such evidence because it would not have contradicted the evidence presented by the Division (see, Laffin v. Ryan, 4 AD2d 21, 162 NYS2d 730).

Petitioner failed to offer clear and convincing evidence to rebut this presumption that he received the excess net profits of the corporations as constructive dividends. Given these circumstances, the Division acted properly in assessing petitioner and its determination was based upon substantial evidence.

Petitioner has failed to carry his burden of proving by clear and convincing evidence that both the method used to arrive at the amounts forming the basis of the assessment and the assessment itself are erroneous (see, Tax Law § 689[e]; Matter of Giuliano v. Chu, supra; Matter of Koren-Di Resta Constr. Co. v. State Tax Commn., 138 AD2d 909, 526 NYS2d 654, lv denied 72 NY2d 805, 532 NYS2d 755).

Not only did petitioner fail to offer books and records to support arguments, some of the evidence he did offer could not be given credence. The application submitted by Intercity for qualification as a bidder, proposer and subcontractor, dated November 25, 1987, at the very end of the period in issue, listed petitioner as a 40% shareholder. The application was signed and submitted on behalf of petitioner's corporation by his son, Joseph Drebin, as vice president. However, the fact that Joseph Drebin subsequently pled guilty to failing to file returns and to pay corporation taxes on behalf of Century and Intercity, and the errors and intentional

misstatements of fact contained on the application, render that application's credibility a nullity.

In the case of a closely-held corporation, such as those here, special scrutiny is required because of the unfettered control exercised by a limited number of shareholders (Roschuni v. Commissioner, 29 TC 1193, 1201-1202, affd 271 F2d 267, 59-2 USTC ¶ 9748, cert denied 362 US 988, 4 L Ed 2d 1021). The record supports the conclusion that both of the closely-held corporations in this case were owned and controlled by petitioner and his son, Joseph. Unfortunately, petitioner herein submitted no evidence with regard to his day-to-day role in the corporations. Such testimony as he did offer was vague, incomplete, evasive and, thus, not credible. It can be concluded from what little facts as are available that Century was a mere "shell" with a license, which Intercity used to enable it to conduct business with the City of New York. Given petitioner's disregard for the corporate entities, his claimed lack of knowledge of their officers, the dates of their existence, his failure to produce books and records, and his claimed lack of knowledge regarding the manner in which tax returns were prepared, even though he was principal owner and stockholder of both corporations, supports the Division's conclusion that Mr. Drebin benefitted from the excess income to the corporations. Taking all of these factors together, including the statement by petitioner's accountant that petitioner gave the money to charity, the Division made a logical assumption that petitioner received the net profits attributed to the corporations. Since the burden of proof is on petitioner herein (Tax Law § 689[e]; 20 NYCRR 3000.10[d][4]), it was incumbent upon him to prove that Intercity's excess income was not received by him as excess wages or as a constructive or actual dividend. Petitioner failed or refused to produce such evidence. Petitioner's complete failure to produce any records is fatal. Since he failed to introduce any credible evidence to refute the Division's theory, we conclude that petitioner received the unreported income as excess wages or as constructive or actual dividends.

We also conclude that the Division acted prudently in assessing the entire constructive dividend/excess income to both petitioner and his son, Joseph, although it can only collect the

tax once.

We agree with the Administrative Law Judge that the Division must deduct from the liability determined herein any amount of the personal tax liability ultimately paid and satisfied by Joseph Drebin pursuant to Audit #D-6364. In this way, the State's interest is protected and petitioner's lack of cooperation and failure to keep and/or produce corporate and financial records will not be rewarded.

We next address the issue of penalties. Petitioner was assessed penalty for substantial understatement of liability pursuant to Tax Law § 685(p) for the years 1985, 1986 and 1987, where it was found he understated his income tax for each of those years. Petitioner has provided absolutely no proof to justify abatement of penalties (see also, 20 NYCRR former 102.7). Therefore, the penalties are sustained.

Next, we address petitioner's claim that the tax asserted for the years 1982, 1983 and 1984 is barred by the statute of limitations. At hearing, petitioner's attorney expressly stated that he was not raising the affirmative defense of the statute of limitations. Accordingly, this defense is waived, and the tax for the years 1982, 1983 and 1984 was properly asserted.

Petitioner's proposed findings of fact and conclusions of law are rejected as not supported by the record.

The determination of the Administrative Law Judge is affirmed for the reasons stated above.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Sol Drebin is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petition of Sol Drebin is denied; and

4. The Notice of Deficiency, dated February 15, 1991, is sustained.

DATED: Troy, New York
March 27, 1997

/s/Donald C. DeWitt
Donald C. DeWitt
President

/s/Carroll R. Jenkins
Carroll R. Jenkins
Commissioner