

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
THOMAS AND MARGARET MOORE	:	DETERMINATION
		DTA NO. 816357
for Redetermination of a Deficiency or for Refund of New	:	
York State and New York City Personal Income Taxes		
under Article 22 of the Tax Law and the Administrative	:	
Code of the City of New York for the Year 1993		
	:	

Petitioners, Thomas and Margaret Moore, 66 Hills Lane, Westport, Connecticut 06880, filed a petition for redetermination of a deficiency or for refund of New York State and New York City personal income taxes under Article 22 of the Tax Law and the Administrative Code of the City of New York for the year 1993.

A hearing was held before Winifred M. Maloney, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on September 8, 1998 at 11:30 A.M., with all briefs submitted by December 4, 1998, which date began the six-month period for the issuance of this determination. Petitioner Thomas R. Moore appeared *pro se* and for Margaret Moore. The Division of Taxation appeared by Terrence M. Boyle, Esq. (Andrew S. Haber, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly disallowed, as unsubstantiated, ordinary business expenses connected with a New York source business for the year 1993.

FINDINGS OF FACT

1. Petitioners, Thomas and Margaret Moore, filed a timely Nonresident and Part-Year Resident Income Tax Return (Form IT-203) and New York City Nonresident Earnings Tax Return (Form NYC-203) for the year 1993. On their Form IT-203, petitioners reported the following items as part of their Federal adjusted gross income of \$457,235.00: wages of \$63,621.00, taxable interest income of \$58.00, dividend income of \$312.00, taxable refunds of state and local income taxes of \$5,646.00, a capital loss of \$3,000.00, Schedule E partnership income of \$400,996.00,¹ other income of \$19,602.00 and a Keogh adjustment to income of \$30,000.00. The New York source income reported on the return consisted of wages of \$63,621.00 and other income of \$19,602.00.² Petitioners subtracted the taxable refund of state and local income taxes of \$5,646.00 and interest income on U. S. government bonds of \$476,129.00 and arrived at a New York adjusted gross income of zero. Petitioners claimed itemized deductions of \$9,997.00. They determined their New York State taxable income to be zero, with zero New York State tax due. Based upon Mrs. Moore's wages of \$63,621.00, petitioners determined the City of New York nonresident earnings tax to be \$286.00. Petitioners determined their total State and City taxes to be \$286.00 and claimed a refund of \$5,713.00 of the reported total State and City taxes withheld.

2. Based on the disallowance of the New York subtraction claimed for interest on U. S. government bonds, the Division of Taxation (“Division”) issued to petitioners an assessment

¹The Schedule E attached to Form IT-203 listed the following four partnerships: Essex, Troy, Beauregard and Steinhardt Partners. The record reveals that Mrs. Moore was the partner in the Beauregard and the Steinhardt Partners partnerships. The identity of the partner in the two remaining partnerships is not part of the record.

²The wages are from Mrs. Moore's employment at Cornell Medical College. The source of the “other income” is not identified on the return.

asserting total tax due in the amount of \$7,054.88, less total tax withheld of \$5,999.00, for a balance due of \$1,055.88. Based on correspondence submitted by petitioners, the assessment was canceled. Petitioners' correspondence submitted in protest of the assessment is not part of the record. Subsequently, petitioners received a refund of \$5,713.00 plus interest.

3. A field audit was commenced on April 11, 1995. Review of the auditor's entries in the Tax Field Audit Record ("audit record") reveals that she made a number of requests to petitioners for copies of their 1992 and 1993 Federal personal income tax returns ("Form 1040") along with all pages of the Schedule K-1s for the partnerships listed on the 1992 and 1993 Schedule E's. However, because petitioners were uncooperative and supplied limited information, the auditor had to request information from third-party sources.³ None of the auditor's requests focused on the other income reported as New York source income.

4. The audit of the year 1992 was discontinued after review of the limited information available. The auditor reviewed the 1993 Form 1040, the 1993 Form IT-203 and the K-1 from Steinhardt Partners and determined that petitioners had incorrectly reported Mrs. Moore's distributive share of partnership income from Steinhardt Partners on both their Federal and State returns. A copy of the 1993 Steinhardt Partners K-1 and its supporting schedules are part of the record. Line 7 of this K-1 lists Other Income of \$2,770,838.15, which is broken down into the following categories: Interest on US Obligations of \$339,613.00, Other Interest Income of \$771,944.33, Dividend Income of \$30,102.73, Other Expenses of \$202,658.42, IRC Section 988 Income (foreign currencies) of \$1,083,003.07, Other Income of \$39,727.08, Net Long-Term Capital Gain of \$15,137.67, Net Short-Term Capital Gain of \$695,282.52 and Net Section 1256

³Petitioners did not submit either the 1992 or 1993 Federal return and submitted partial K-1s. The auditor requested both the 1992 and 1993 Federal income tax returns from the I.R.S. However, only the 1993 return was supplied by the I.R.S.

Losses of \$1,313.83.

5. The auditor prepared and sent petitioners a total of three statements of personal income tax audit changes. The majority of the audit adjustments made in the three statements pertained to accounting for various items included in Mrs. Moore's distributive share of the Steinhardt Partners income. Subsequent to the issuance of the first statement, petitioners submitted additional information which formed the basis of the second statement. As a result of the correspondence submitted by petitioners challenging the second statement, the third and final Statement of Personal Income Tax Audit Changes was issued on August 30, 1996. In that Statement of Personal Income Tax Audit Changes, the auditor made the following adjustments: increased the Federal adjusted gross income by \$2,281,859.22 to a total of \$2,739,094.22; increased the Federal itemized deductions by \$876,026.61; increased the New York State addition modification by \$239,991.14; decreased the New York State subtraction modification by \$136,516.00 and increased the New York State allowable itemized deductions by \$433,014.81. As a result of the audit adjustments, petitioners' New York State taxable income was determined to be \$2,190,814.56 and the base New York State tax on that amount was determined to be \$172,526.65. The auditor then multiplied the New York State income percentage of 3.04%⁴ by the base New York State tax of \$172,526.65, determining the recomputed New York State tax to be \$5,244.81. No additional New York City earnings tax was determined to be due. The statement issued showed a corrected tax liability for New York State in the amount of \$5,244.81 and for New York City in the amount of \$286.00. Penalty for negligence under Tax Law § 685(b), equal to 5% of the additional tax due, plus interest were added to the additional tax

⁴The auditor determined the New York State income percentage by dividing the State adjusted gross income of \$83,223.00 by Federal adjusted gross income of \$2,739,094.22.

asserted as due.

In the cover letter which accompanied the third statement of audit changes, the auditor addressed the issues raised in petitioners' letter challenging the second statement of audit changes and explained the slight revisions to the previous computation of petitioners' Federal and New York taxable income which were reflected in the final statement. The auditor also indicated that any applicable revisions would be made to petitioners' Federal and New York taxable income if a copy of the complete K-1 from the Troy⁵ partnership was submitted. Petitioners did not submit any response to the August 30, 1996 Statement of Personal Income Tax Audit Changes.

6. Subsequently, the Division issued a Notice of Deficiency, dated October 21, 1996, for personal income taxes due pursuant to Article 22 of the Tax Law for the year 1993 in the amount of \$5,244.81, plus interest of \$1,126.08 and penalties of \$825.28. No additional City of New York nonresident earnings tax was asserted. The computation section of the notice contained the following explanation "The following tax is computed as a result of the recent audit of your records. This tax is being assessed in accordance with the Statement of Proposed Audit Adjustments previously sent to you."

7. According to the August 21, 1997 entry in the auditor's tax field audit record, petitioners filed a request for a conciliation conference, stating the basis for disagreement as the following: "Taxpayer has no federal adjusted gross income from New York sources for 1993 and therefore, no New York tax liability."

8. A Bureau of Conciliation and Mediation Services ("BCMS") conciliation conference took place on October 6, 1997. According to the entry in the audit record for that date, Mr.

⁵The name of the partnership is spelled two ways in the record: "Troy" and "Troye." It is unclear which is the correct spelling.

Moore came to the conciliation conference with an amended Form IT-203 for 1993 which increased the Federal adjusted gross income, but decreased New York source income. Mr. Moore did not have any supporting documentation for the amended return nor did he have a copy of the amended Federal return because it had yet to be completely prepared or filed with the Internal Revenue Service. The entry further states that the nature of the other income was first revealed during the conciliation conference when Mr. Moore stated that the other income was from his law practice conducted in New York City and that the correct net income from his law practice was a loss of \$91,814.00 for Federal and New York State purposes. The auditor refused to accept the amended Form IT-203 without substantiation. The auditor's notes also indicate that the conferee gave her permission to request information from petitioners and to set up an appointment to review their records.

9. Another auditor met with Mr. Moore at his office on October 29, 1997. At that meeting, a general discussion about Mr. Moore's legal practice took place. The audit record indicates that Mr. Moore explained that he had been in practice for approximately seven years and, in some of those years, he actually had positive net income. The auditor noted that Mr. Moore described his work as mostly "contingent," whereby if he recovers money or puts deals together (i.e., investment banking deals), he receives either a finder's fee or a percentage of the money recovered. Mr. Moore noted that he handled other types of cases, but was not specific as to the nature of those matters. He further stated that if the money was not recovered or the deal was not consummated, he might not bill his client and just absorb the expenses. According to the auditor's notes, Mr. Moore maintained two checking accounts: one at the Bank of New York, account number 0951308998, in which all of his receipts were deposited and the other, a Dreyfus money market account in which distributions from his partnerships were deposited.

Copies of the Bank of New York checking account statements were not provided.

10. The second auditor's notes indicate that, during that meeting, Mr. Moore provided an original "amended 1993 IT-203" to be filed through the Division's Buffalo District Office, but did not supply a copy of the amended Federal 1993 return because it was not yet completed. The notes also indicate that he submitted the following handwritten schedules: a Profit and Loss statement; "a list of receipts (clients);" a breakdown of all other business expenses (legal and other); a breakdown of office rent paid and copies of his American Express statements, indicating business meals deducted. The notes indicate that copies of canceled checks for most of the expenses, including those payments made to HQ Business Center for his office rent, were submitted. The notes also indicate that amounts paid to HQ included fees for secretarial, postage and other miscellaneous office expenses.

At the conclusion of the meeting, the auditor requested additional information in order to verify the receipts amount claimed, as well as the legal expenses claimed. Mr. Moore was requested to supply the following items within two weeks: copies of all invoices billed to clients; all invoices received from law firms for services provided to Mr. Moore and copies of the Bank of New York checking account statements.

11. The record includes a handwritten worksheet, for 1993, given to the auditor at the October 29, 1997 meeting. This worksheet contains the computation of the claimed loss of \$100,641.00 from Mr. Moore's business. The calculation follows: first, office rent in the amount of \$51,094.00 was subtracted from fees received in the amount of \$70,696.00; then, office expenses (legal) in the amount of \$34,756.00 and office expenses (general) in the amount of \$85,487.00 were subtracted from the remainder of \$19,602.00 to arrive at a loss of \$100,641.00.

12. By letter dated November 18, 1997, the conciliation conferee informed petitioners

that, based on all the evidence submitted at the conciliation conference, he had determined as follows:

The starting point for determining New York State income tax is federal adjusted gross income. As you have not filed an amended federal income tax return, and are prohibited from filing such amended return by the three year statute of limitations, the basis of your New York income tax for the year 1993 is your federal AGI as originally filed.

You are also prohibited from filing an amended New York State personal income tax return by the three year statute of limitations under Section 687 of the New York Tax Law. Therefore, your amended New York State IT-203 return is not accepted.

The conferee also informed petitioners that since they had not submitted any evidence to refute the audit findings, he had to sustain the Notice of Deficiency.

13. By letter dated November 28, 1997, Mr. Moore challenged the conferee's determination, writing the following:

1. No New York tax is due for 1993 because we had no New York taxable income. This was proven in papers I submitted to Amy Sahr of the New York State Department of Taxation in a face-to-face conference on October 29, 1997 and in back-up documents I submitted at her request to Dianne Di Pasquale on November 6, 1997. Both agreed in a telephone conference that no tax is due.

2. With due deference, I submit your reading of Section 687 is incorrect. Section 687(a) prohibits a claim for *refund after* the 3-year statute has run. It does not prohibit a showing of the true facts when a *deficiency* is being resisted. Furthermore, the New York 3-year statute has *not* run because the State has kept it open by instituting this procedure. Section 687(b) and (f). If any tax had been paid, a refund would be due.

3. Please expunge the asserted deficiency and send me notice to that effect.

14. The conferee issued a Conciliation Order (CMS No. 159092) dated December 12, 1997 sustaining the statutory notice.

15. Petitioners filed a petition challenging the Notice of Deficiency. In their petition, petitioners assert that no tax is due because they had no New York source income; rather they

had a loss of \$67,020.00. They further assert that because there is no tax due, the adjustments proposed by the Division, relating to non-New York source income, “while erroneous, are irrelevant.” Attached to the petition is a “pro forma” amended Form IT-203, which claims a loss of \$100,641.00 as other income in the Federal and New York State columns, as well as a Keogh adjustment in the New York State column. Review of this “pro forma” amended return indicates that the amounts listed in the Federal column as: wages, taxable interest income, dividend income, taxable refunds of state and local income taxes, capital loss and Schedule E partnership income were the amounts reported on petitioners' original return (*see*, Finding of Fact “1”). The amount listed in the New York State column as wages is also the same amount as was reported on the original return filed (*see*, Finding of Fact “1”). On this “pro forma” amended return, the Federal adjusted gross income - New York amount is listed as zero and no New York modifications, deductions or exemptions are listed.

16. In support of their position that, as nonresidents, they do not owe any taxes to New York State for 1993, petitioners presented petitioner Thomas R. Moore as their sole witness. Mr. Moore explained that, in 1993, the amount reported as the net short-term gain from partnerships, on the Federal Schedule D, line 5, included the deduction of \$111,416.00 in ordinary business expenses, properly allocable against New York source income, which he inadvertently failed to deduct from the amounts shown on the New York State return as New York source income on line 16. Mr. Moore stated that the additional ordinary business expenses properly allocable to New York source income consisted of office rent in the amount of \$51,094.00, legal expenses in the amount of \$34,640.00 and general office expenses of \$25,682.00. Mr. Moore's testimony consisted of general statements concerning the amounts claimed as his ordinary business expenses. He did not offer any testimony about each expense item and how it related to his legal

practice. His testimony also did not include any specific information about his legal practice.

17. In addition to Mr. Moore's testimony, petitioners submitted a total of five affidavits along with supporting documentation, consisting of three affidavits of petitioner Thomas R. Moore and the affidavits of Colleen Susini and Barbara Cooper.

18. Two of Mr. Moore's affidavits reiterate the statements he made at the hearing concerning the claimed ordinary business expenses. In the third affidavit, Mr. Moore averred that, in 1993, he “deducted \$51,094 of miscellaneous business expenses on [his] federal income tax return and allocated such \$51,094 against New York State income on [his] New York State return.” The documents attached to the affidavit include (1) a summary schedule which lists total credit card charges for claimed business expenses by month, amounts paid to a trustee in bankruptcy and amounts paid for research and Christmas gifts; (2) 16 monthly statements for Visa and American Express accounts (“summary of account statements”) issued to Mr. Moore and (3) a copy of the three-page 1993 year-end summary of deposits, reinvestments and check redemptions⁶ for the Dreyfus money market account in the name of “Thomas R Moore TTE, FBO R H Moore Tr, U/T/D 11/13/78” (“Dreyfus transaction summary statement”).

Review of the summary of account statements indicates that the claimed business expenses included charges from restaurants, the majority of which were located in New York, as well as air line and hotel charges for travel and lodging within and without the United States. Handwritten notations appear next to some of the charges on the various statements. The notations include the names of some of the individuals and a corporation, the words “Bus Lunch” or “Bus Meal” and the letter “B.” On some statements, only the notation “Pers” appears next to a

⁶The checks are listed by number only, not named payee.

few entries. None of the source documents relating to the credit card charges are part of the record. Mr. Moore did not testify about each individual travel and entertainment charge.

As noted above, while the Dreyfus transaction summary statement does list the dates and amounts of check redemptions, it does not list the named payee. Handwritten notations appear next to some of the check redemptions. The handwritten notation "Court & Tru"⁷ appears next to check redemption number 111, in the amount of \$4,881.58. Other check redemptions, numbers 115 and 104, in the amounts of \$1,000.00 and \$3,222.00, respectively, contain the handwritten notation "Research." The record does not include any source invoices pertaining to the payments claimed to have been made for research or any source documents concerning the payment claimed to have been made to a trustee in bankruptcy. No checks drawn on the Dreyfus money market account are part of the record.

19. Ms. Susini is the office manager of HQ. In her affidavit, Ms. Susini states that "[D]uring 1993 Thomas R. Moore paid office rent of \$51,094 to HQ." Attached to the Susini affidavit are the following supporting documents: a handwritten document entitled "Ledger, 1993, Office Rent," which lists the amounts paid to HQ by month; a copy of two pages of the 1993 Dreyfus transaction summary statement and a page containing photocopies of two canceled checks, payable to HQ, drawn on Mr. Moore's Bank of New York checking account. On the Dreyfus transaction summary statement, nine amounts are circled and a handwritten "HQ" appears next to the circled amount. As noted above, none of the Dreyfus checks are part of the record. The record also does not include invoices or source documents relating to the rental of office space from HQ or its address.

⁷Only the letters "Tru" are legible, the remainder of the word is totally illegible.

20. In support of claimed legal services rendered on behalf of Mr. Moore's legal practice, the affidavit of Barbara Cooper with attachments was submitted. Ms. Cooper is the administrative assistant to Gerald Ross, managing partner of the firm of Fryer & Ross, known prior to April 30, 1994 as Fryer, Ross & Gowen. In her affidavit, Ms. Cooper states, in pertinent part, as follows:

2. We have represented and continue to represent Thomas R. Moore in connection with various matters relating to his law practice from September 1992 to the present.

3. Our client records show that Mr. Moore paid us \$34,630.61 for legal services rendered and disbursements incurred on his behalf with respect to his law practice during the period January 1, 1993 through December 31, 1993.⁸

Attached to Ms. Cooper's affidavit are: a single typewritten sheet entitled "Ledger, 1993, Office Expenses - Legal" which lists amounts paid to Fryer, Ross & Gowen in the months of January, April, July, September, October and December, (\$5,392.00; \$2,000.00; \$2,313.00; \$3,671.00; \$1,695.00 and \$19,569.00, respectively), totaling \$34,640.00; copies of seven canceled checks payable to Fryer, Ross & Gowen drawn on Mr. Moore's Bank of New York account totaling \$34,638.61;⁹ and 7 invoices, dated December 28, 1992, April 2, 1993, June 10, 1993, July 7, 1993, September 9, 1993, October 12, 1993 and November 15, 1993, respectively, from the law firm of Fryer, Ross & Gowen, addressed to Thomas R. Moore, Esq., 930 Fifth Ave., Suite 900, New York, New York. Each invoice lists the period covered and contains a breakdown of the total amount due for professional services rendered by "Professional Services" and "Disbursements." There is no further identification of the specific matter for which the

⁸At the hearing, Mr. Moore noted that Ms. Cooper's affidavit contained an error, that he actually paid the Fryer, Ross & Gowen law firm \$34,640.00.

⁹The reference section of each of the checks is blank.

professional services were rendered.

21. The record includes photocopies of approximately 53 checks drawn on Mr. Moore's Bank of New York account submitted in support of the claimed general office expenses in the amount of \$25,682.00. The claimed office expenses include, among others, payments totaling \$3,525.78 to the University Club,¹⁰ payments to petitioner Margaret K. Moore totaling \$8,963.16,¹¹ and a payment to Al Togut Liquidation Trustee in the amount of \$4,481.58.¹² The invoices or source documents relating to the claimed general office expenses are not part of the record. No further explanation concerning the various claimed general office expenses was offered.

22. The record does not include a list of clients or any invoices pertaining to legal work claimed to have been performed by Mr. Moore during the period in issue.

23. During the hearing, the auditor stated that the Schedule K-1s were requested for all partnerships listed on the Federal return. Petitioners did not submit all of the K-1s. The auditor explained that, based on the reported ID numbers for the other three partnerships, she determined that they were not New York source businesses. She further stated that, with respect to the other three partnerships, she accepted the amounts reported as filed.

24. In response to the question whether she had ever asked Mr. Moore what figures went into the net amount which was reported on the Federal Schedule D, line 5, the auditor responded “[S]pecifically not that line.” (Tr., p. 39.)

¹⁰No notations appear in the memo section of any of the twelve checks payable to the University Club.

¹¹The record includes two checks, numbered 1161 and 1241, respectively, payable to Mrs. Moore, each in the amount of \$4,481.58. The following notation appears in the memo section of check #1161 [in dark ink] “Reimb: Re Trustee in Bankruptcy.” Check # 1241 contained the following notation “re Musselman Trustee in Bankruptcy.”

¹²This check does not contain any notation in the check's memo section.

25. At the conclusion of the hearing, petitioners requested that the record remain open to afford them the opportunity to submit a document showing how the figure on Schedule D, line 5 was computed, specifically the flow of the deductions in issue. Petitioners' request was granted.

26. Petitioners did not submit any additional documentary evidence. The record in this matter closed on September 22, 1998.

SUMMARY OF THE PARTIES' POSITIONS

27. In their brief, petitioners assert that the Notice of Deficiency issued in this matter should be canceled. They contend that they have shown that the New York State income of \$83,223.00 “was eliminated by \$111,416 of New York State deductions taken on their 1993 Federal return but inadvertently not shown on line 16 of their New York State return.” (Petitioners' brief, p. 1.) Petitioners maintain that they incorrectly netted the \$111,416.00 of New York source business expense deductions against non-New York source short-term income from partnerships on line 5 of Schedule D rather than deducting these business expenses from New York source income. They argue that these deductions, consisting of office rent of \$51,094.00, legal expenses of \$34,640.00 and general office expenses of \$25,682.00, relate to a business carried on in New York, i.e., Mr. Moore's legal practice, the income from which they reported as other income on line 16 of the Form IT-203. Petitioners contend that the allowance of these additional expenses results in a loss of \$91,814.00 from Mr. Moore's legal practice rather than the \$19,602.00 of income originally reported as other income. They maintain that the loss from Mr. Moore's practice eliminates the additional New York source income of \$63,621.00 and there is no New York State income subject to tax.

Alternatively, petitioners argue that the Notice of Deficiency should be canceled because New York law does not permit a second audit. They maintain that they

filed a refund claim for 1993 taxes withheld, which, after audit, were refunded, as had been the case for 1992. When the Auditor began this second audit of 1992 and 1993, Petitioners raised the legal point that New York State law does not permit second audits. The Auditor thereupon withdrew the second audit of 1992, but not the second audit of 1993 because the Auditor deemed Petitioners “uncooperative” in pressing their point . . . and even after repeatedly agreeing in writing that Petitioners had “no net New York State income” . . . the Auditor continued the case. (Petitioners' brief, p. 2.)

28. In its brief, the Division points out that petitioners do not dispute its audit findings that they did not properly report income from the Steinhardt Partners partnership. Turning to petitioners' claim that additional ordinary business expenses should be deducted from Mr. Moore's business income as an attorney, the Division argues that petitioners have failed to prove that any claimed expenses were business related.

29. In their reply brief, petitioners state that the “controversy about the income from Steinhardt Partners is *immaterial* since both parties agree that it was not NY source income.” (Petitioners' reply brief, p. 1; emphasis in original.) They argue that they have proven that all of the ordinary business expenses were related to Mr. Moore's practice of law in New York State. Therefore, petitioners assert that Mr. Moore had a loss from his legal practice rather than the profit originally reported on the 1993 nonresident return as other income.

CONCLUSIONS OF LAW

A. Petitioners are not challenging the audit adjustments made with respect to the income from the Steinhardt Partnership. Rather, they claim that they inadvertently deducted New York source business expenses from non-New York source short-term income from partnerships and reported the net gain on line 5 of the Federal Schedule D. They argue that the ordinary business expenses, totaling \$111,416.00, were connected with Mr. Moore's legal practice, a New York business, and therefore, were properly deductible from the amount reported as other income on

line 16 of their 1993 nonresident income tax return..

B. During the period in issue, Tax Law § 631 provided, in pertinent part, as follows:

(a) General. The New York source income of a nonresident individual shall be the sum of the net amount of items of income, gain, loss and deduction entering into his federal adjusted gross income, as defined in the laws of the United States [Internal Revenue Code] for the taxable year, derived from or connected with New York sources,

(b) Income and deductions from New York sources.

(1) Items of income, gain, loss and deduction derived from or connected with New York sources shall be those items attributable to:

* * *

(B) a business, trade, profession or occupation carried on in this state

Because the deduction would be included in arriving at Federal adjusted gross income (IRC § 62[a][1]), Federal law is controlling authority in deciding this question (*see, Matter of Rizzo v. Tax Appeals Tribunal of the State of New York*, 210 AD2d 748, 621 NYS2d 115). IRC § 162(a) requires that three conditions be satisfied before a deduction is allowed for a claimed business expense. The expense must be: (1) incurred in carrying on a trade or business; (2) ordinary and necessary; and (3) paid or incurred within the taxable year.

C. Pursuant to Tax Law § 689(e) it is concluded that petitioners have failed to sustain their burden of proving that the claimed business expenses are connected with Mr. Moore's legal practice. This failure is based upon a lack of adequate substantiation of the business purpose of the claimed deductions. Petitioners' evidence consisted of Mr. Moore's testimony, affidavits and documents. Mr. Moore's testimony consisted of vague general statements about the claimed business expenses (*see*, Finding of Fact "16"). Mr. Moore offered no explanation of the nature of the legal expenses which he claims were incurred with respect to his legal practice. He also did

not testify about any of the claimed entertainment and travel charges listed on the monthly credit card statements. Nor did he explain the nature of the University Club charges and their business purpose. The documentary evidence submitted as proof of the claimed office rent expense, the miscellaneous expenses (entertainment and travel charges) and the general office expenses consists of summary ledger sheets, monthly credit card statements, the Dreyfus transaction summary statement and photocopies of canceled checks. No source documentation was submitted to support the summary schedules, the credit card statements, the Dreyfus transaction summary statement, or the canceled checks (*see*, Findings of Fact “18,” “19” and “21”). Ms. Cooper's affidavit, the canceled checks and the invoices from the law firm of Fryer, Ross & Gowen do establish that Mr. Moore paid legal expenses totaling \$34,638.61. However, because the invoices fail to state the matters for which the services were rendered, it is impossible to determine whether the claimed legal expenses were incurred with respect to matters pertaining to Mr. Moore's legal practice.

In sum, petitioners have failed to prove that the ordinary business expenses are connected with a New York source business rather than non-New York partnerships as petitioners originally reported on their 1993 Federal and New York State non-resident returns.

D. Petitioners have been assessed penalties pursuant to Tax Law § 685(b) for negligence. Petitioners bear the burden of proving that their failure to pay the correct amount of tax for 1993 was due to reasonable cause and not due to negligence (Tax Law § 685[b]; § 689[e]). Petitioners did not raise, argue or present any evidence on this issue. Since petitioners have not presented any evidence tending to show that their failure to pay the correct amount of tax was due to reasonable cause, the negligence penalty assessed pursuant to Tax Law § 685(b) must be sustained (*see, Matter of Albanese*, Tax Appeals Tribunal, July 17, 1997; *Matter of Gucci*, Tax

Appeals Tribunal, July 10, 1997).

E. Alternatively, petitioners argue that the Notice of Deficiency in this matter should be canceled because New York law does not permit a second audit or the issuance of a second notice of deficiency. They have not supported their argument with any statutory authority or case law.

Petitioners' argument is without merit. Tax Law § 682(d) provides for the issuance of a supplemental assessment, in pertinent part, as follows:

[t]he [commissioner of taxation and finance] may, at any time within the period prescribed for assessment, make a supplemental assessment subject to the provisions of section six hundred eighty-one where applicable, whenever it is ascertained that any assessment is imperfect or incomplete in any material respect.

The notice at issue is a result of a determination by the auditor that petitioners incorrectly reported income received from the Steinhardt Partnership. The petition which initiated the present proceeding challenges that Notice of Deficiency. Tax Law § 689(d)(4) provides that, once a taxpayer has filed a petition with the Division of Tax Appeals, the Division of Taxation may not issue any further notices of deficiency for the same taxable year, except in the case of fraud or with respect to a change or correction required to be reported under Tax Law § 659. There is no evidence that petitioners filed a petition with the Division of Tax Appeals after the first assessment was issued. The only petition filed challenges the Notice of Deficiency dated October 21, 1996.

Petitioners have failed to prove that the Division's issuance of the Notice of Deficiency was erroneous.

F. The petition of Thomas and Margaret Moore is denied and the Notice of Deficiency dated October 21, 1996 is sustained.

DATED: Troy, New York
May 27, 1999

/s/ Winifred M. Maloney
ADMINISTRATIVE LAW JUDGE