

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition

of

ARTHUR A. RESTANI

DECISION

for Redetermination of a Deficiency or for  
Refund of Personal Income and Unincorporated :  
Business Taxes under Articles 22 and 23 of the  
Tax Law for the Years 1975 through 1977.

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Petitioner, Arthur A. Restani, 204 Maple Lane, North Syracuse, New York 13212, filed a petition for redetermination of a deficiency or for refund of personal income and unincorporated business taxes under Articles 22 and 23 of the Tax Law for the years 1975 through 1977 (**File No.** 30976).

A hearing was held before Arthur Bray, Hearing Officer, at the offices of the State Tax Commission, 333 East Washington Street, Syracuse, New York, on April 3, 1985 at 10:00 A.M., with all briefs to be submitted by June 19, 1985. Petitioner appeared by George S. Howlett, Esq. The Audit Division appeared by John P. Dugan, Esq. (James Della Porta, Esq., of counsel).

#### ISSUES

I. Whether petitioner is entitled to claim a series of miscellaneous deductions.

II. Whether the Audit Division properly redetermined petitioner's gross profit percentage on the installment sale of a restaurant.

#### FINDINGS OF FACT

1. Petitioner owned and operated a restaurant known as Art's Town House from approximately 1959 through 1976. On October 1, 1976, petitioner sold the restaurant on the installment basis

2. Petitioner filed a New York State Income Tax Resident Return for 1975. This return was neither accompanied by a New York State Unincorporated Business Tax Return nor a schedule C, encaptioned Profit or (Loss) from Business or Profession.

3. Petitioner filed a New York State Income Tax Resident Return for 1976. Petitioner attached to this return a New York State Unincorporated Business Tax Return, a Federal schedule C encaptioned Profit or (Loss) from Business or Profession, and a schedule disclosing the installment sale of the restaurant. The unincorporated business tax return and the Federal schedule C were for the period January 1, 1976 through September 29, 1976. The unincorporated business tax return stated that an unincorporated business tax return was not filed for the year 1975 because petitioner had insufficient income. On this return, petitioner reported the installment sale of the restaurant. In determining the amount of the gain on the installment sale of the restaurant, petitioner treated real estate fees and attorney fees as fully deductible items in the year of the sale.

4. Petitioner filed a New York State Income Tax Resident Return for the year 1977. On this return, petitioner reported gain from the installment sale of the restaurant.

5. On April 11, 1980, the Audit Division issued a Notice of Deficiency to petitioner asserting tax due in the amount of \$5,929.45, plus penalty and interest in the amount of \$1,464.69, for a total amount due of \$7,394.14. To the extent at issue herein, the Notice of Deficiency was premised upon recomputing the amount of gross income which petitioner was required to recognize each year from the sale of the restaurant. The recomputation arose from disallowing real estate fees and legal fees as current deductible expenses.

expenses be prorated over the term of the installment sale. The Audit Division also disallowed, in whole or in part, certain business expenses claimed by petitioner. The penalty was asserted pursuant to section 685(c) of the Tax Law for nonpayment or underpayment of estimated tax.

6. Notices and demands for payment of sales and use taxes due were issued to Art's Town House as follows<sup>1</sup>:

<u>Date of Notice</u>	<u>Period</u>	<u>Tax</u>	<u>Penalty and Interest</u>	<u>Total</u>
August 20, 1976	August 31, 1975	\$2,640.87	\$686.12	\$3,326.99
August 20, 1976	November 30, 1975	2,442.84	488.30	2,931.14
August 20, 1976	February 29, 1976	2,230.23	312.90	2,543.13
November 5, 1976	August 31, 1976	3,161.96	238.57	3,400.53

7. Petitioner substantiated that during 1977 he made payments of sales tax in satisfaction of his liability in the amount of \$8,700.00.

8. After the Notice of Deficiency was issued, the Audit Division reduced the amount of the tax asserted due in the Notice of Deficiency of personal income tax by \$137.16 based upon interest expense incurred and paid in 1977 on the sales tax assessments in the amount of \$1,036.14.

9. During the years in issue, petitioner's financial records were prepared on a cash basis system of accounting. The tax returns were prepared by an accountant named William F. Hurley. Petitioner testified that it was Mr. Hurley's practice to include the sales tax collected as part of the restaurant's gross receipts and then reduce the restaurant's business gross income by the sales tax as the sales tax was paid. No books, records or documentation were presented to substantiate this proposition.

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1 On May 24, 1976, a Notice of Determination and Demand for Payment of Sales and Use Taxes Due was issued to Art's Town House for the period ending February 29, 1976. This was superseded by the Notice of Deficiency dated August 1, 1976.

10. After the restaurant was sold, petitioner continued to satisfy outstanding expenses of the restaurant. Since the unincorporated business tax return filed for 1976 was for the period January 1, 1976 through September 29, 1976, the business expenses incurred after the sale of the restaurant were not reflected on petitioner's tax return. At the hearing, petitioner submitted sufficient substantiation that he incurred during 1976 the following expenses, which were not reflected on his tax return:

<u>Check Number</u>	<u>Date</u>	<u>Payee</u>	<u>Amount</u>
7459	10/12/76	Stewart Jones	\$ 325.00
7468	12/13/76	Altmann Bottling Co., Inc.	54.08
7469	12/13/76	Netti Wholesale Beverages, Inc.	253.73
7470	12/13/76	Onondaga Products Corporation	391.55
7471	12/13/76	Monarch Liquor Corporation	377.68
7472	12/13/76	S & K Wine & Liquor Corp.	104.98
7473	12/13/76	McKesson Wine & Spirits Co.	132.00
7474	12/13/76	Delia & Smith Beverage Corp.	47.00
7475	12/13/76	Syracuse Wine & Spirit Co.	82.32
7476	12/13/76	Colonie Liquor of Syracuse, Inc.	124.12
7477	12/13/76	M. Lichtman & Co., Inc.	66.53
7478	12/15/76	Chairman-Workmen's Compensation Board	1,792.55
7480	12/21/76	Central Restaurant Supply, Inc.	300.00
			<u>\$4,051.54</u>

11. The record contains sufficient substantiation to establish that petitioner **is** entitled to the following deductions which were not reflected on his tax return for 1977:

<u>Check Number</u>	<u>Date</u>	<u>Payee</u>	<u>Amount</u>
238	7/14/77	Richards "Of Course"	\$167.04
298	10/21/77	DeFelsko Corp.	607.43
			<u>\$774.47</u>

12. The record does not contain any substantiation to support the following proposed deductions:

<u>Check Number</u>	<u>Date</u>	<u>Payee</u>	<u>Amount</u>
7466	10/29/76	New York Telephone Company	\$ 136.04
nnt provided			

13. In addition to the foregoing, petitioner has sought a deduction of \$304.50 based upon a payment to George S. Howlett, Esq. for legal services. Petitioner also sought a deduction for interest paid on a promissory note from Marine Midland Bank. However, no evidence was presented as to the portion of the payment which represented interest and the portion which represented principal. Lastly, petitioner sought a deduction in the amount of \$141.58 based upon a check dated August 14, 1979 payable to the order of City Restaurant Supply.

14. In 1984, the purchaser of the restaurant began defaulting on the installment payments. On this basis, petitioner has requested that the expenses of the sale which were prorated over the course of the installment payments should be permitted as current period deductions.

#### CONCLUSIONS OF LAW

A. That sales taxes are collected by a vendor as a trustee (Tax Law §1132[a]; see Canale v. New York State Dept. of Taxation and Finance, 84 A.D.2d 786, 789). The funds collected belong to New York State as the beneficiary of the trust (Canale v. New York State Dept. of Taxation and Finance, supra). Consequently, the sales tax collected did not constitute part of the restaurant's gross receipts. Conversely, the sales tax remitted to New York State did not constitute a business expense.

B. That in view of the fact that petitioner's tax returns were prepared by an accountant and that no books, records or other documents were presented to establish that petitioner was treating the sales tax collected as part of the gross receipts and the sales tax remitted as a business expense, petitioner has failed to sustain his burden of proof of establishing that the gross receipts were overstated by the amount of the sales tax collected.

C. That petitioner has not sustained his burden of proof of establishing that he is entitled to a deduction for interest on the sales tax assessments beyond that which has been agreed to by the Audit Division (Finding of Fact "8"). It is impossible to determine from the record presented the portion of the assessment which represents penalty and that portion which represents deductible interest.

D. That petitioner has substantiated the business expenses incurred in 1976 and 1977 as described, respectively, in Findings of Fact "10" and "11" (Tax Law §689[e]). Accordingly, the Notice of Deficiency issued April 11, 1980 is to be adjusted accordingly.

E. That petitioner has not established that he is entitled to the deductions described in Findings of Fact "12" and "13". It is noted that the proposed deduction of \$304.50 based upon the payment to George S. Howlett, **Esq.** for legal services is rejected since it is not possible to discern from the record whether this was part of the expense incurred with respect to the sale of the restaurant and should therefore have been prorated over the payment period. In addition, no deduction for payment on a promissory note in the amount of \$1,135.08 is permitted since the record does not establish the portion of the payment which represents interest and the portion which represents principal. Further, since petitioner was a cash basis taxpayer, petitioner is not entitled to a deduction during the years in issue for the check drawn to the order of City Restaurant Supply dated August 14, 1979.

F. That since petitioner elected to utilize the installment method of reporting the sale of the restaurant, the Audit Division properly determined that the attorney fees and real estate fees could not be deducted in the year of the sale (T.R.C. §453(b); Treas. Reg. §§1.453-1(f)(1), 1.453-1(f)(2)).


gross profit to determine the proportion of installment payments recognized as income (Treas. Reg. §§1.453-1[b]). It is noted that when a purchaser defaults on his installment payments, there is **no** provision in the Internal Revenue **Code** **for** retroactively recomputing the amount of gain or **loss on** an installment sale as **if no** installment sale had occurred (See generally 3B Rabkin & Johnson, Federal Income, Gift and Estate Taxation, 543.12, p. 4393, et. seq.).

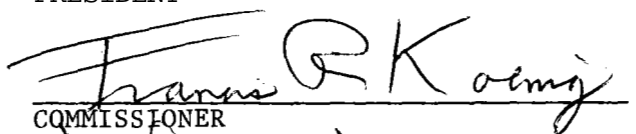
G. That the petition of Arthur A. Restani is granted to the extent of Conclusion of Law "D" and the Audit Division is directed to recompute the Notice of Deficiency as modified in Finding of Fact "8" accordingly. The petition is, in all other respects, denied and, as modified, the Notice of Deficiency **is** sustained.

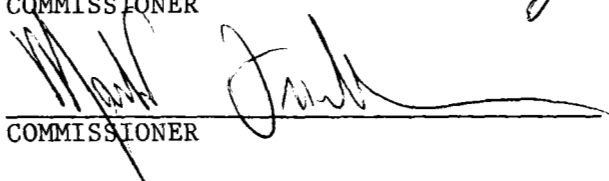
DATED: Albany, New York

STATE TAX COMMISSION

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COMMISSIONER

  
COMMISSIONER