

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petitions

of

:

FRED DREYSPRING

DECISION

for Redetermination of a Deficiency or for  
Refund of New York State Personal Income Tax  
under Article 22 of the Tax Law and New York  
City Nonresident Earnings Tax under Chapter 46,  
Title U of the Administrative Code of the City :  
of New York for the Years 1978 and 1979.

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Petitioner, Fred Dreyspring, 53-A Heritage Hills, Somers, New York 10589,  
filed a petition for redetermination of a deficiency or for refund of New York  
State personal income tax under Article 22 of the Tax Law and New York City  
nonresident earnings tax under Chapter 46, Title U of the Administrative Code  
of the City of New York for the years 1978 and 1979 (File Nos. 37542 and  
42987).

On October 23, 1985, petitioner waived his right to a hearing and requested  
the State Tax Commission to render a decision based on the entire record contained  
in his file, with all briefs to be submitted by October 8, 1986. After due  
consideration, the State Tax Commission hereby renders the following decision.

ISSUES

I. Whether the notices of deficiency were issued without any basis and  
for the sole purpose of extending the period of limitation on assessment.

II. Whether petitioner has substantiated that he was engaged in a trade or  
business during the years at issue.

III. Whether petitioner has substantiated the character and amount of  
business expenses claimed as deductions from gross income for the years at  
issue.

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FINDINGS OF FACT

1. For the year 1978, petitioner, Fred Dreyspring, together with his wife, JoAnn Dreyspring, filed a New York State Income Tax Resident Return, with New York City nonresident earnings tax, wherein they elected a filing status of "Married filing separately on ~~one~~ Return". On his portion of said return, petitioner reported business income of \$23,914.00. The following table details the manner in which petitioner computed his business income on his Federal Schedule C attached to the return:

FRED DREYSPRINGIncome

Sales consultant	\$42,698.00
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Expenses

Travel	\$ 718.00	
Dry cleaning	98.00	
Valet	151.00	
Luggage	174.00	
Travel aids	43.00	
Car rental	270.00	
Dues and subscriptions	151.00	
Books, research and reference	412.00	
Telephone	278.00	
N.Y.S. Council of Pharm. Meetings	286.00	
Hospitality	1,827.00	
Sports with clients	772.00	
Meetings and interviews	803.00	
Writing supplies for pamphlets	49.00	
Secretarial	10,200.00	
Newspapers, magazines, etc.	309.00	
Postage	35.00	
Dictating supplies	257.00	
Professional development	692.00	
Training of sales help	984.00	
Accounting	275.00	
Total Expenses		<u>18,784.00</u>
Net Income		<u><u>\$23,914.00</u></u>

2. Attached to petitioner's return were wage and tax statements issued **to** Mr. Dreyspring by Ayerst Labs Div. of American Home Products Corp. reporting wages, tips, other compensation of \$42,698.38. The statements were stamped with an arrow pointing to figures totalling \$42,698.38 with the legend "Included in Schedule C" . The \$10,200.00 secretarial expense claimed by Mr. Dreyspring was paid to his wife. Mrs. Dreyspring reported this amount **in** "other income" **on** her return. The 1978 return listed petitioner's occupation as "sales consultant" and reported \$26,158.00 in total income, consisting of \$1,828.00 in interest, \$176.00 in dividends, \$23,914.00 in business income and \$240.00 from the sale or exchange of capital assets.

3. On March 26, 1982, the Audit Division issued a Statement of Audit Changes **to** petitioner and his spouse for the year 1978 which contained the following explanation:

"We have reviewed your 1978 personal income tax return and find the following:

The expenses claimed **on** Federal Schedule C are not ordinary or necessary in the production of income as an employee; therefore, all Schedule C expenses are disallowed.

You are not considered subject to unincorporated business income. A credit for maximum tax credit is applicable and is included in the following recomputation.

	<u>Husband</u>	<u>Wife</u>		
Wages reported on Wage and Tax Statements			\$42,698.38	\$-0-
	<u>Husband</u>	<u>Wife</u>		
Interest	\$1,828.00	\$473.00		
Dividend	176.00	176.30		
Capital asset	<u>240.00</u>	<u>240.00</u>	22,244.00	889.00
Total income			\$44,942.38	\$889.00
Less: Itemized deduction			<u>9,808.00</u>	-0-
Balance			\$35,134.38	\$889.00
Less: Exemptions			<u>1,300.00</u>	650.00
Corrected Taxable Income			\$33,834.38	\$239.00 "

4. Based on the aforementioned Statement of Audit Changes, the Audit Division, on April 14, 1982, issued a Notice of Deficiency to petitioner for 1978 asserting additional New York State personal income tax and New York City nonresident earnings tax due of \$1,813.03, plus interest of \$523.01, for a total allegedly due of \$2,336.04. The amount allegedly due included a credit due to Mrs. Dreyspring for 1978 of \$475.95 ( $\$2,288.98 - 475.95 = \$1,813.03$ ).

5. For the year 1979, petitioner, Fred Dreyspring, together with his wife, JoAnn Dreyspring, timely filed a New York State Income Tax Resident Return, with New York City nonresident earnings tax, wherein they elected a filing status of "Married filing separately on one return". On his portion of said return, petitioner reported business income of \$24,983.00. The following table details the manner in which petitioner computed his business income on his Federal Schedule C:

FRED DREYSPRING

Income

Sales consultant	\$45,648.00
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Expenses

Travel	\$ 903.00
Dry cleaning	298.00
Valet	204.00
Luggage	139.00
Travel aids	45.00
Car rental	350.00
Dues and subscriptions	259.00
Books, research and reference	563.00
Telephone	300.00
N.Y.S. Council of Pharm. Meetings	125.00
Hospitality	2,621.00
Sports with clients	583.00
Meetings and interviews	983.00
Writing supplies for pamphlets	141.00
Secretarial	10,200.00
Newspapers, magazines, etc.	398.00
Postage	153.00
Dictating supplies	630.00
Professional development	478.00

Training of sales help	1,017.00	
Accounting	275.00	
Total Expenses		<u>20,665.00</u>
<u>Net Income</u>		<u>\$24,983.00</u>

6. Attached to petitioner's return were wage and tax statements issued to Mr. Dreyspring by Ayerst Labs Div. of American Home Products Corp. reporting wages, tips, other compensation of \$45,647.88. The statements were stamped with an arrow pointing to the figures totalling \$45,647.88 with the legend "Included in Schedule C". The \$10,200.00 secretarial expense claimed by Mr. Dreyspring was paid to his wife. Mrs. Dreyspring reported this amount as "other income" on her return. The 1979 return listed petitioner's occupation as "sales consultant" and reported \$28,162.00 in total income consisting of \$788.00 in interest, \$218.00 in dividends, \$24,983.00 in business income and \$2,173.00 in capital gains.

7. On February 7, 1983, the Audit Division issued a Statement of Audit Changes to petitioner and his spouse for the year 1979 which contained the following explanation:

"As a salaried employee, you are not a business entity and therefore are not entitled to claim Schedule C deductions as these expenses are not ordinary and necessary for the production of income as an employee.

	<u>Husband</u>	<u>Wife</u>
Total income corrected	\$48,826.88	\$3,182.00
Add: Capital Gain Modification	<u>11.00</u>	<u>11.00</u>
Total New York income corrected	\$48,837.88	\$3,182.00
Less: Itemized deductions	<u>9,758.00</u>	<u>          </u>
Balance	\$39,079.88	
Less: Exemptions	<u>700.00</u>	<u>700.00</u>
New York Taxable Income	\$38,379.88	\$2,493.00"

8. Based on the aforementioned Statement of Audit Changes, the Audit Division, on April 8, 1983, issued a Notice of Deficiency to petitioner for

1979 asserting additional New York State personal income tax and New York City nonresident earnings tax due of \$2,316.30, plus interest of \$769.93, for a total allegedly due of \$3,086.23. The amount allegedly due included a credit due to Mrs. Dreyspring for 1979 of \$590.65 ( $\$2,906.95 - \$590.65 = \$2,316.30$ ).

9. Petitioner's tax return was selected for examination along with those of approximately 100 other individuals on the basis that the returns had been prepared by a particular accountant. An investigation had disclosed that said accountant had consistently prepare# returns on which an individual with wage or salary income shown on wage and tax statements had reported said income as business receipts on Federal Schedule C. Department of Taxation and Finance auditors were directed to review the returns and to disallow claimed business expense deductions if the taxpayer appeared to be an employee receiving wage or salary income reported on wage and tax statements. Petitioner's claimed Schedule C deductions were disallowed on that basis.

10. Petitioner submitted documentary evidence in the form of sales invoices, cancelled checks and worksheets in substantiation of a portion of the business expenses claimed on his Federal Schedule C. However, the evidence submitted did not relate to a characterization of the expenses as business rather than personal.

11. Petitioner contends:

(a) that the notices of deficiency were issued on an arbitrary and capricious basis just prior to the expiration of the period of limitations on assessment, thus depriving petitioner of the opportunity to present substantiation for the claimed deductions;

(b) that petitioner is one of a large group of taxpayers who were selected for special scrutiny because their returns had been prepared by the same tax preparer; and

(c) that where petitioner does not have cancelled checks or other receipts for certain expenses, the Department of Taxation and Finance should allow petitioner a reasonable estimate of such expenses.

CONCLUSIONS OF LAW

A. That the notices of deficiency were properly issued and were not arbitrary and capricious. The returns were patently erroneous and the Audit Division was justified in disallowing the business expenses claimed by petitioner on his Federal Schedule C's. The notices of deficiency were preceded by statements of audit changes and petitioner had an opportunity to file amended returns claiming employee business expenses as adjustments to income on Federal Form 2106, or as itemized miscellaneous deductions, but did not do so.

B. That the fact that petitioner's returns were selected for examination because of certain practices of his accountant is irrelevant. Petitioner's liability depends solely on the facts adduced herein.

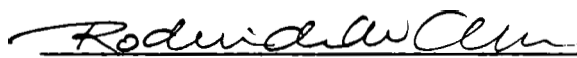
C. That petitioner has failed to sustain his burden of proof (Tax Law § 685[e]; Administrative Code § T46-189.0[e]) to show (i) that he was engaged in a trade or business other than as an employee (Internal Revenue Code § 62[1]); (ii) that the expenses in question were trade or business deductions of employees deductible pursuant to Internal Revenue Code § 62(2); and (iii) that the expenses in question were ordinary and necessary business expenses deductible under Internal Revenue Code § 162(a).

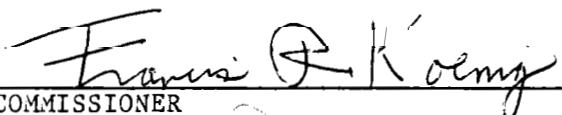
D. That the petitions of Fred Dreyspring are denied and the notices of deficiency dated April 14, 1982 and April 3, 1983 are sustained in full, together with such additional interest as may be lawfully due and owing.


DATED: Albany, New York

STATE TAX COMMISSION

APR 06 1987

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER