

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

JOHN GEBHARDT

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 Personal Income Tax under Chapter 46 ,
Title T of the Administrative Code of the City :
of New York for the Years 1978 and 1979.

Petitioner, John Gebhardt, 305 East 24th Street, Apartment 4C, New York, New York 10010, 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 personal income tax under Chapter 46, Title T of the Administrative Code of the City of New York for the years 1978 and 1979 (File Nos. 37563 and 42967).

On October 23, 1985, petitioner waived a hearing before the State Tax Commission and agreed to submit the matter for decision based on the Audit Division file, as well as a brief and additional documents to be submitted by October 8, 1986. After due consideration of the record, 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.

FINDINGS OF FACT

1. Petitioner, John Gebhardt, filed New York State income tax resident returns with City of New York personal income tax for 1978 and 1979. **His** wife, Frances Gebhardt, filed separately on the same returns. On each return, petitioner's occupation was stated to be "Author Educator" while his wife's was stated as "Researcher".

2. The 1978 return.

(a) For 1978, petitioner reported \$14,172.00 in business income and no wage or salary income.

(b) Petitioner filed a Federal Schedule C, Form 1040, showing the following income and expenses:

"INCOME - English Chairmen's Assn.	\$ -0-
English Program - (see W-2)	
Russian Program - (see W-2)	
Board of Examiners (separate pay included in W-2)	
	<u>\$22,909</u>
Travel USSR (American Field Services - Continuation of 1977 teaching program) Easter recess: 10 days	\$2,382
Russian books, magazines, records etc.	600
Union dues & other professional memberships	300
Accounting	115
Study Allocation: Work for Board of Examiners' exam preparations, President of English Chairmen's Assn., Russian library, storage of Russian phonograph records, tapes, slides, photographs & teaching material that is not property of Board of Education	
20% alloc. of apt. x \$656 (Rent \$610 + electric \$46)	
= 130 x 12 = 1,560	1,560
Auto Travel: For Board of Examiners, interview candidates for teaching positions, transport own books and teaching materials, trips to other schools to collect books needed etc.	
7300 mi. @ 17¢	1,241

Tolls	85	
Unreimbursed departmental expense - Jan & June		
'78 parties	375	
Cab fares - parking	260	
Professional development - dramatic events plays, films, ballet functions re: USSR & admissions		
72nd Street Cinema etc.	1,069	
Hosting Russian Counterparts of AFS program - welcoming committee	750	
Damage to clothes in hotel laundry 4/78		
Total loss - shrank		
		8,737
		<u>\$14,172"</u>

The schedule did not show a "Main business activity".

(c) Attached to the return was a wage and tax statement issued by The City of New York Board of Education, showing that petitioner had "Wages, and other compensation" of \$22,909.29. Federal, State and local income taxes and FICA were withheld.

(d) .Petitioner and his wife itemized deductions, claiming \$1,153.00 in miscellaneous deductions, all of which were attributable to and taken by petitioner's wife.

(e) Petitioner filed a New York State Unincorporated Business Tax Return for 1978, on which he reported net profit of \$14,172.00. A note on the return indicated that said sum represented "Wages subject to FICA tax included in Schedule C". An allowance for taxpayer's services of 20% (\$2,834.00) reduced net income from business to \$11,338.00. After the \$5,000.00 exemption, taxable business income was shown as \$6,338.00 and \$258.63 in unincorporated business tax was shown as due.

3. The 1979 return.

(a) For 1979, petitioner reported \$14,876.00 in business income and no wage or salary income.

(b) Petitioner filed a Federal Schedule C, Form 1040, showing the following income and expenses:

"INCOME: Classroom Teaching	\$ 9,200	
Program Development	13,307	
Board of Examiners	1,000	
American Field Services	<u>-0-</u>	\$23,507
EXPENSES:		
Subscriptions to Soviet magazines	237	
Russian/English programs: books	392	
Books, records, slides:		
English poets/Scottish plays & playwrights;		
inspection of schools, educational travel	1,492	
Newspapers, magazines	311	
Accounting	125	
Dues & subscriptions	416	
Professional development: drama events, slides films	1,937	
Hosting & meetings with counterparts, curriculum		
development	971	
Local travel	292	
Automobile (7,250 mi. @ 18½¢)	1,341	
Tolls & parking	183	
Postage & mailings		
N.CTE Convention - S.F., Cal.	<u>934</u>	\$ 8,631
NET INCOME		<u>\$14,876,,</u>

The schedule did not show a "Main business activity".

(c) Attached to the return was a wage and tax statement issued to petitioner by The City of New York Board of Education., showing \$23,506.96 in "Wages, tips, other compensation". A stamped arrow with the legend "Included in Schedule C" pointed to said figure. As in 1978, Federal, State and local income taxes and FICA were withheld. Pension plan coverage was also shown.

(d) Petitioner and his wife itemized deductions and claimed \$1,224.00 in miscellaneous deductions, all of which were attributable to and taken by petitioner's wife.

(e) Petitioner filed a New York State Unincorporated Business Tax Return for 1979, showing \$14,876.00 in net profit and subtractions of \$23,507.00.

A stamped arrow with the legend "FICA wages included in Schedule C" pointed to the subtractions. This resulted in a net loss from business of \$8,631.00 and no tax was shown as due.

4. Petitioner's tax returns were selected for examination along with those of approximately 100 other individuals on the basis that said returns had been prepared by a particular accountant. An investigation had disclosed that said accountant had consistently prepared 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.

5. (a) On March 24, 1982, the Audit Division issued a Statement of Audit Changes to petitioner for 1978 with the following explanation:

"Income shown on wage and tax statements is considered to be wages and reportable as such on page 2, Schedule A, at line 1.

Expenses claimed on Schedule C (Business income) are not considered to be ordinary and necessary in the production of income as an employee.

Unincorporated business tax is recomputed to zero."

A total of \$920.12 in New York State and New York City taxes was asserted.

(b) On April 14, 1982, the Audit Division issued a Notice of Deficiency to petitioner for 1978 asserting \$920.12 in additional tax due, plus interest.

6. (a) On January 17, 1983, the Audit Division issued a Statement of Audit Changes to petitioner for 1979, with 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."

Since recomputed New York taxable income was over \$21,000.00, petitioner was allowed a maximum tax benefit. Additional New York State and New York City taxes of \$1,251.38 were asserted.

(b) On April **8**, 1983, the Audit Division issued a Notice of Deficiency to petitioner for \$1,251.38 in additional tax, plus interest.

7. Petitioner was assistant principal of Fort Hamilton High School in Brooklyn, New York, during the years at issue. He also taught English at the school. It appears that he was involved with Russian studies or Russian language studies at the school, but the exact nature and extent of his involvement **is** not clear from the record.

8. Petitioner traveled to Russia for 8 days in 1978 and to England and Scotland for 21 days in 1979. The cost of each trip was deducted on the Schedule C filed for each year (Findings of Fact "2[b]-- and "3[b] ").

9. Petitioner submitted documentary evidence substantiating the following deductions:

- a. For 1978, \$276.00 in union dues, \$72.90 in other dues and \$100.00 in tax preparation fees.
- b. For 1979, \$300.00 in union dues, \$140.50 in other dues and \$100.00 in tax preparation fees.

10. 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 part 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 a reasonable estimate of such expenses.

CONCLUSIONS OF LAW

A. That the notices of deficiency were properly issued and were not arbitrary or capricious. The returns were patently erroneous and the Audit Division was justified in disallowing the Schedule C business income and expenses. Each Notice of Deficiency was preceded by a Statement of Audit Changes and petitioner had an opportunity to file amended returns claiming employee business expenses as adjustments 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 not sustained his burden of proof under section 689(e) of the Tax Law and Administrative Code § T46-189.0(e) to show that he was engaged in a trade or business other than as an employee. Thus, expenses claimed on Schedule C may not be deducted under section 62(1) of the Internal Revenue Code.

D. That petitioner may deduct the \$348.90 in dues and \$100.00 in tax preparation fees as miscellaneous deductions for 1978, and \$440.50 in dues and \$100.00 in tax preparation fees as miscellaneous deductions for 1979. While it would appear that petitioner may have been entitled to deduct certain other employee business expenses under sections 62(2) or 63(f) of the Internal Revenue

Code if he had filed form **2106**, or if he had claimed such expenses as miscellaneous itemized deductions, petitioner nevertheless failed to sustain his burden of proof under the Tax Law and Administrative Code to show the character or, in many cases, the amount **of** the claimed business expenses.

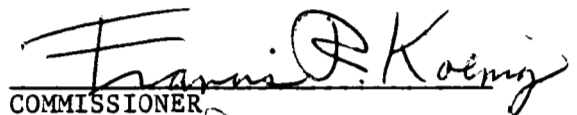
E. That the petition of John Gebhardt **is** granted to the extent provided in Conclusion of Law "D"; that the Audit Division **is** hereby directed to modify the notices of deficiency issued on April 14, 1982 and April 8, 1983, accordingly; and that except as **so** granted, the petition is in all other respects denied.

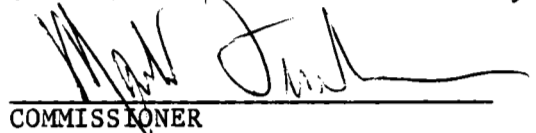
DATED: Albany, New York

STATE TAX COMMISSION

MAY 26 1987

PRESIDENT


COMMISSIONER


COMMISSIONER