

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petitions

of

FRANK ~~NASTASI~~ AND KATHLEEN NASTASI

DECISION

for Redetermination of Deficiencies or for Refunds of New York State and New York City Personal Income Taxes under Article 22 of the Tax Law and Chapter 46, Title T of the Administrative Code of the City of New York for the Years 1978 and 1979.

Petitioners, Frank Nastasi and Kathleen Nastasi, 21 Piedmont Avenue, Staten Island, New York 10305, filed petitions for redetermination of deficiencies or for refunds of New York State and New York City personal income taxes under Article 22 of the Tax Law and Chapter 46, Title T of the Administrative Code of the City of New York for the years 1978 and 1979 (File Nos. 37612 and 44440).

On October 23, 1985, petitioners waived their right to a hearing and requested the State Tax Commission to render a decision based on the entire record contained in their 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 Frank Nastasi was engaged in a trade or business during the years at issue.

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

FINDINGS OF FACT

1. Petitioners, Frank Nastasi and Kathleen Nastasi, filed a New York State Income Tax Resident Return for the year 1978 wherein they elected a filing status of "Married filing separately on one Return". Petitioners claimed a standard deduction on this return.

2. To the extent at issue herein, the 1978 New York State return listed Frank Nastasi's occupation as "Construction Contractor". Mr. Nastasi reported that his total income included business income of \$9,376.00. Mrs. Nastasi reported that she had other income of \$5,200.00.

(a) A copy of the Federal Schedule C, entitled Profit (or Loss) from Business or Profession, for Frank Nastasi reported income of \$19,806.00, consisting of income from Blomeley Engineering of \$19,556.00 and income from subcontracting of \$250.00. Mr. Nastasi then listed the following expenses:

Payments to Kathleen Nastasi	\$ 5,200.00
Dues	595.00
Accounting	100.00
Arctic Wear	183.00
Telephone	120.00
Travel expense	1,483.00
Tolls	110.00
Parking	158.00
Solicitation, meetings	1,274.00
Tools	264.00
Materials	502.00
Clean-up & carting	421.00
	<u>\$10,430.00</u>

The \$10,430.00 in expenses deducted from income of \$19,806.00 resulted in the \$9,376.00 net business income reported.

(b) A wage and tax statement issued to Mr. Nastasi and attached to the return showed "Wages, tips, other compensation" of \$19,555.88 from Insulation Service System, Inc. The statement was stamped with an arrow pointing to the \$19,555.88 figure with the legend "Included in Schedule C".

(c) The New York State Unincorporated Business Tax Return of Frank Nastasi reported a net profit and total income from business before New York modifications of \$9,376.00. This amount was reduced by \$19,556.00 resulting in a loss of \$10,180.00.

3. Petitioners filed a U.S. Individual Income Tax Return for the year 1978 wherein they elected a filing status of "married filing joint return (even if only one had income)". Petitioners did not itemize their deductions on this return.

4. Petitioners filed a New York State Income Tax Resident Return for the year 1979 wherein they elected a filing status of "Harried filing joint return". Petitioners claimed the standard deduction when preparing the return. To the extent at issue herein, the 1979 New York State tax return listed Frank Nastasi's occupation as "Construction Contractor" and reported business income of \$15,817.00

(a) A copy of the Federal Schedule C for Mr. Nastasi for 1979 reported income of \$31,028.00 as follows:

Insulation Service System	\$27,584.00
Beach Electric	2,041.00
Interest	753.00
Subcontractors	650.00
	<u>\$31,028.00</u>

(b) The Federal Schedule C for 1979 reported expenses of \$15,211.00

Payments to Kathleen Nastasi (Office Asst.)	\$ 5,200.00
Dues & memberships	696.00
Accounting	150.00
Arctic wear & outside rain gear	317.00
Telephone	240.00
Travel Exp.	3,050.00
Tolls	118.00
Parking	154.00
Solicitation, meetings	2,196.00
Tools	393.00
Materials	697.00
Clean-up & carting	725.00
Telephone & Messenger Svce.	
J. N.	650.00
Telephone outside	482.00
Magazines, newspapers (re: following constr. market)	143.00
	<u>\$15,211 .00</u>

The \$15,211.00 in expenses deducted from the income of \$31,028.00 resulted in the \$15,817.00 net business income reported.

(c) The wage and tax statements attached to petitioner's return showed "Wages, tips., other compensation" from Beach Electric Co., Inc. of \$2,040.57 and "Wages, tips, other compensation" of \$27,584.30 from Insulation Service System. Each statement was stamped with an arrow pointing to, respectively, the \$2,040.57 and \$27,584.30 figures with the legend "Included in Schedule C" .

(d) Frank Nastasi filed a New York State Unincorporated Business Tax Return for 1979 which reported net profit of \$15,817.00 less subtractions of \$29,625.00 resulting in a net **loss** of \$13,808.00. The unincorporated business tax return was stamped with an arrow pointing to the \$29,625.00 figure with the legend "FICA wages included in Schedule C".

5. The record **does** not contain information as to whether petitioners filed a Federal income tax return for 1979.

6. Petitioners' tax returns were selected for examination along with those of approximately 100 other individuals on the list of

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. Petitioners' claimed Schedule C deductions were disallowed on that basis.

7. On April 14, 1982, the Audit Division issued a Notice of Deficiency to petitioners asserting a deficiency of New York State and New York City personal income tax for the year 1978 in the amount of \$749.27, plus penalty of \$149.84 and interest of \$230.00, for a balance due of \$1,129.11. A Statement of Audit Changes, which was issued on the same day, explained that the expenses claimed on the Federal Schedule C were not allowed since they were not "ordinary and necessary in the production of income as an employee". Further, the amount of tax due was computed on a joint basis, to petitioners' advantage, since the \$5,200.00 of wage expense to Mrs. Nastasi was not allowed.

8. On February 8, 1983, the Audit Division issued a Statement of Audit Changes to petitioners explaining that they had a deficiency of New York State and New York City personal income tax for the year 1979. The explanation provided was that, as a salaried employee, Mr. Nastasi was not entitled to claim deductions on a Federal Schedule C. On April 8, 1983, the Audit Division issued a Notice of Deficiency to petitioners for the reason set forth above asserting a deficiency of tax in the amount of \$1,637.76, plus interest of \$544.39, for a balance due of \$2,182.15.

9. Upon the submission, the only evidence presented was groups of cancelled checks, receipts, letters, copies of tax returns and written descriptions of activities and expenses incurred. However, the evidence submitted is insufficient to establish (i) that Frank Nastasi was engaged in the carrying on of a trade or business (other than as an employee); (ii) that the expenses constituted employee trade or business deductions; and (iii) that the expenses constituted ordinary and necessary business expenses and not personal expenditure:

10. Petitioners contend:

(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 petitioners of the opportunity to present substantiation for the claimed deductions;

(b) that petitioners are 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 petitioners do not have cancelled checks or other receipts for certain expenses, the Department of Taxation and Finance should allow petitioners 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 Frank Nastasi on his Federal Schedules C.

B. That the fact that petitioners' returns were selected for examination because of certain practices of their accountant is irrelevant. Petitioners' liability depends solely on the facts adduced herein.

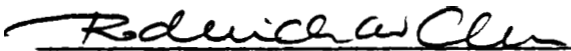
C. That petitioners have failed to sustain their burden **of** proof (Tax Law § 689[e]; Administrative Code § T46-189.0[e]) to show (i) that Frank Nastasi was engaged in a trade or business other than as an employee (Internal Revenue Code § 62[1]); (ii) that the expenses in question were trade or business deductions **of** employees deductible pursuant to Internal Revenue Code § 162; and (iii) that the expenses in question were ordinary and necessary business expenses deductible under Internal Revenue Code § 162(a). It is noted that since petitioners did not itemize their deductions on their Federal tax return for 1978 or show that they itemized their deductions on their Federal tax return for 1979, petitioners are not entitled to claim any **of** the items listed on their Federal Schedules C as itemized deductions (Tax Law § 615[a]).

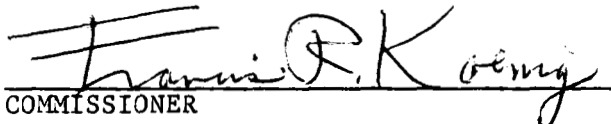
D. That the petitions **of** Frank Nastasi and Kathleen Nastasi are denied and the notices **of** deficiency dated April 14, 1982 and April 8, 1983 are sustained in full, together with such additional interest and penalties as may be lawfully due and owing.

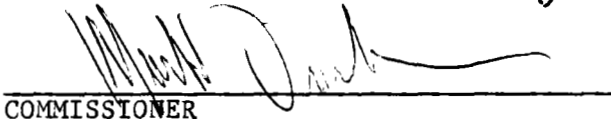
DATED: Albany, New York

STATE **TAX** COMMISSION

MAY 29 1987


PRESIDENT


COMMISSIONER


COMMISSIONER