

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

DRAGUTIN NIKOLIC and ELENA NIKOLIC

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 Year 1978.

Petitioners, Dragutin Nikolic and Elena Nikolic, 81 Hylan Boulevard, Staten
Island, New York 10305, 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 Administra
Code of the City of New York for the Year 1978 (File Nos. 37759 and 38102).

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 Dragutin Nikolichas substantiated that he was
engaged **in** a trade **or** business during the year at issue.

III. Whether petitioner Dragutin Nikolic has substantiated the character
and amount of business expenses claimed as deductions from **gross** income for the

FINDINGS OF FACT

1. Petitioners, Dragutin Nikolic and Elena Nikolic, timely filed a New York State and City income tax resident return for 1978 wherein they elected a filing status of "Married filing separately on one Return". On his portion of said return, Mr. Nikolic reported business income of \$13,742.00, while on her portion of the return Mrs. Nikolic reported wages and interest income totalling \$8,052.00. The following table details the manner in which Mr. Nikolic computed his business income:

| <u>Income</u> | | |
|--------------------|-----------------|-------------|
| Narrows Tanker | \$14,800.00 | |
| Anway Distributors | -0- | |
| Delivery Charges | -0- | |
| Emergency Service | <u>3,831.00</u> | |
| Total Income | | \$18,631.00 |

| <u>Expenses</u> | | |
|--|---------------|--|
| Purchases | \$ 639.00 | |
| Delivery & Travel | 841.00 | |
| Telephone | 180.00 | |
| Samples | 193.00 | |
| Postage | 51.00 | |
| Mailings | 52.00 | |
| Work Clothes: | | |
| Rain Wear | 120.00 | |
| Arctic Wear | 62.00 | |
| Gloves | 245.00 | |
| Safety Shoes | 158.00 | |
| Recruiting Costs | 198.00 | |
| Tools | 233.00 | |
| Northwestern Rain Hats | 15.00 | |
| Travel - Delivery of Anway Products ordered & paid in 1977: | | |
| 2200 miles @ .17 | 374.00 | |
| Long Distance Telephone | 292.00 | |
| Meals on Board: 16 weeks @ 7 days = 112 days @ 10.00 = \$1,120.00 | | |
| Reimbursed 112 days @ \$6.00 = \$672.00 | 448.00 | |
| Travel to Boat - 16 Roundtrips @ \$15.00 | 240.00 | |
| Dues | 250.00 | |
| Magazines & Newspapers | 198.00 | |
| Accounting | <u>100.00</u> | |

| | |
|-------------------|--------------------|
| Total Expenses | <u>\$ 4,889.00</u> |
| <u>Net Income</u> | \$13,742.00 |

2. Attached to petitioners' 1978 return was a wage and tax statement issued to Mr. Nikolic by Narrows Tanker Corp. reporting "wages, tips, other compensation" of \$18,630.54. The statement is stamped with an arrow pointing to the \$18,630.54 figure with the legend "Included in Schedule C".

3. On March 22, 1982, the Audit Division issued a Statement of Audit Changes to petitioners for the year 1978 which contained the following explanation:

"We have reviewed your 1978 income tax return and have disallowed business expenses as shown on Schedule C. The expenses claimed are not necessary and ordinary in the production of income as an employee.

Since your total household gross income is over \$25,000.00, the household credit is not allowed."

4. The Audit Division recomputed petitioners' New York State and City income tax liability for 1978 as follows:

| | <u>Husband</u> | Wife |
|------------------------------------|-----------------|------------|
| New York taxable income per return | \$ 9,928.00 | \$7,402.00 |
| Expenses disallowed | <u>4,889.00</u> | <u>-0-</u> |
| New York taxable income corrected | \$14,817.00 | \$7,402.00 |

| | <u>State</u> | | city | |
|-------------------------|----------------|---------------|----------------|---------------|
| | <u>Husband</u> | Wife | <u>Husband</u> | Wife |
| Tax on above | \$843.53 | \$284.12 | \$315.69 | \$122.25 |
| Tax per original return | <u>427.46</u> | <u>266.62</u> | <u>182.20</u> | <u>122.25</u> |
| | \$416.07 | \$ 17.50 | \$153.49 | -0- |

5. Based on the aforementioned Statement of Audit Changes, the Audit Division, on April 6, 1982, issued notices of deficiency to petitioners for 1978 asserting additional New York State and City tax due as indicated above, plus interest.

6. Petitioners' tax return was selected for examination along with those

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 Dragutin Nikolic's claimed Schedule C deductions were disallowed on that basis.

7. Petitioner Dragutin Nikolic submitted documentary evidence in the form of receipts, 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.

8. 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 petitioners were 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 did 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**

Division was justified in disallowing the business expenses claimed by Dragutin Nikolic **on** his Federal Schedule C. The notices of deficiency were preceded by a Statement of Audit Changes and Mr. Nikolic had an opportunity to file an amended return 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 petitioners' return was 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 Dragutin Nikolic 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** an employee 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).

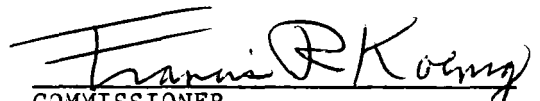
D. That the petition of Dragutin Nikolic and Elena Nikolic **is** denied and the notices **of** deficiency dated April 6, 1982 are sustained in full, together with such additional interest as may be lawfully due and owing.


DATED: Albany, New York

STATE TAX COMMISSION

APR 15 1987


PRESIDENT


COMMISSIONER


COMMISSIONER