

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

RUDOLPH OCELLO AND BARBARA OCELLO

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.

Petitioners, Rudolph Ocello and Barbara Ocello, 240-24 Weller Avenue, Rosedale, New York 11422, 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. 37760 and 43256).

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 Barbara Ocello has substantiated that she was engaged in a trade or business during the years at issue.

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

FINDINGS OF FACT

1. Petitioners, Rudolph Ocello and Barbara Ocello, filed a New York State Income Tax Resident Return for 1978 wherein they elected a filing status of "Harried filing joint Return". Petitioners filed a New York State Income Tax Resident Return for the year 1979 wherein they elected a filing status of "Married filing separately on one return". Barbara Ocello filed New York State unincorporated business tax returns for 1978 and 1979.

(a) To the extent at issue herein, the 1978 New York State tax return listed Barbara Ocello's occupation as "Finishing Service". Petitioners reported that their total New York income included business income of \$1,074.00.

(i) A copy of the Federal Schedule C for Barbara Ocello, captioned "Profit or **(Loss)** From Business or Profession", reported income of \$3,514.00 and listed the following expenses:

Materials to practice on	\$ 498.00
Telephone	240.00
Travel to get work	975.00
Accounting	100.00
Newspapers, magazines	118.00
Tools	130.00
Sewing machine	150.00
Samples	126.00
Sewing patterns, etc.	103.00
Total expenses	<u>\$2,440.00</u>

The \$2,440.00 in expenses deducted from income of \$3,514.00 resulted in the \$1,074.00 net business income reported.

(ii) A wage and tax statement issued to Barbara Ocello and

from Stephen Guida Co., Inc. The statement was stamped with an arrow pointing to the \$3,513.55 figure with the legend "Included in Schedule C" .

(iii) The New York State Unincorporated Business Tax Return of Barbara Ocello for 1978 reported a net profit and total income from business before New York modifications of \$1,074.00. This amount was reduced by \$3,531.00 resulting in a loss of \$2,457.00.

(b) The 1979 New York State Income Tax Resident Return listed Barbara Ocello's occupation as "Finishing Service" and reported her total income of \$1,052.00, which consisted of interest income of \$19.00 and business income of \$1,033.00.

(i) The Federal Schedule C for Barbara Ocello showed income from garment finishing of \$4,597.00 and expenses of \$3,564.00' as follows:

Payments to Anthony Ocello for messenger service	\$1,200.00
Materials, trimmers, notions	496.00
Telephone - inside & outside	120.00
Travel to get work	843.00
Accounting	100.00
Newspapers, magazines	327.00
Tools	204.00
Sewing machine maint.	103.00
Samples	113.00
Sewing patterns, etc.	108.00

The \$3,564.00 in total expenses deducted from revenues of \$4,597.00 resulted in the \$1,033.00 net business income reported.

(ii) A wage and tax statement issued to Barbara Ocello and attached to the return showed \$4,597.07 in "Wages, tips, other compensation" from Stephen Guida Co., Inc. Like the 1978 statement, a stamped arrow with the Legend "Included in Schedule C" pointed to said compensation.

(iii) The New York State Unincorporated Business Tax Return of Barbara Ocello for 1979 reported a net profit and total income from business before New York modifications of \$1,033.00. This amount was reduced by \$4,597.00 resulting in a loss of \$3,564.00.

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

3. (a) On March 22, 1982, the Audit Division issued a Statement of Audit Changes to petitioners asserting a deficiency of New York State and New York City personal income tax for the year 1978. The explanation of the proposed adjustment was that the "[a]mount deducted as Schedule C expenses is not considered ordinary and necessary expense in production of income earned as an employee." The Audit Division recomputed the tax on a separate basis since it resulted in a lower tax liability. On April 6, 1982, the Audit Division issued a Notice of Deficiency to Rudolph Ocello asserting a deficiency of New York State and New York City personal income tax for the year 1978 in the amount of \$678.84, plus interest of \$193.81, for a total amount due of \$872.65. On the same date, the Audit Division issued a Notice of Deficiency to Barbara Ocello

asserting a deficiency of New York State and New York City personal income tax in the amount of \$111.48, plus interest of \$31.83, for a total amount due of \$143.31.

(b) On February 8, 1983, the Audit Division issued a Statement of Audit Changes to Barbara Ocello with respect to the year 1979 explaining that, as a salaried employee, she was not entitled to claim deductions on a Federal Schedule C since the deductions were not ordinary and necessary for the production of income as an employee. On April 8, 1983, the Audit Division issued a Notice of Deficiency against Barbara Ocello asserting a deficiency of New York State and New York City personal income tax for the year 1979 in the amount of \$149.46, plus interest of \$49.67, for a total amount due of \$199.13.

4. Upon the submission, the only evidence presented with respect to the expenses claimed was copies of petitioners' tax returns during the years in issue and an affidavit stating that the expenses reported on the Schedule C were incurred. The evidence submitted is insufficient to establish (i) that Barbara Ocello 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 expenditures.

5. 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

(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 Barbara Ocello on her Federal Schedule C. The notices of deficiency were preceded by statements of audit changes and petitioners had an opportunity to file amended returns claiming employee business expenses as adjustments on Federal Form 2106, or as additional miscellaneous deductions, but did not do so.

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 Barbara Ocello 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).

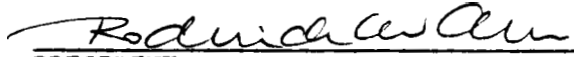
D. That the petitions of Rudolph Ocello and Barbara Ocello are denied and the notices of deficiency dated April 6, 1982 and April 8, 1983 are sustained

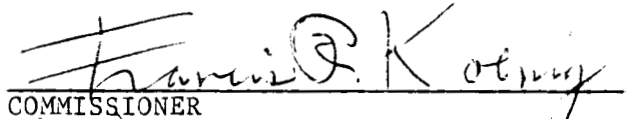
in full, together with such additional interest as may be lawfully due and owing.

DATED: Albany, New York

STATE TAX COMMISSION

JUN 09 1987


PRESIDENT


COMMISSIONER


COMMISSIONER