

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petitions

of

DePAUL TRUNK AND VIRGINIA TRUNK

DECISION

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

Petitioners, DePaul Trunk and Virginia Trunk, 10 Rolling Ridge Road,
Rudolph, New Jersey 07801, filed petitions for redetermination of deficiencies
or for refunds of New York State personal income tax under Article 22 of the
Tax Law and City of New York 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. 37766 and 44355).

On October 23, 1985, petitioners advised the State Tax Commission that
they desired to waive their right to hearing and to submit their case for
decision based upon the existing record contained in the file, together with
the submission of additional evidence by October 8, 1986. After due considera-
tion, 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 petitioners have substantiated that they were 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. For the years 1978 and 1979, DePaul Trunk and Virginia Trunk, filed a joint New York State income tax nonresident returns with City of New York nonresident earnings tax. DePaul Trunk also filed unincorporated business tax returns for said years.

(a) The 1978 return listed DePaul Trunk's occupation as a marketing consultant and Virginia Trunk's occupation as an office aide, although she reported **no** income for said year. Therefore, for the year 1978, all references to "petitioner" shall refer solely to DePaul Trunk. On his 1978 return, petitioner reported total income of \$49,060.00, consisting of \$46,783.00 wages, \$108.00 interest income, \$1,942.00 business income and \$227.00 other income. Petitioner claimed to have worked a total of 237 days for the year, 190 of which were worked **in** New York State. He, therefore, allocated approximately 80 percent of his wage income to New York State plus 100 percent of his business income and his other income, for a total New York income of \$39,674.00.

(i) The copy of the Federal Schedule C attached to the return indicated income from petitioner's business or profession as a marketing consultant consisting of \$9,075.00 from a percentage of consulting revenues and \$865.00 from sales for Fischer Medical Publications, Inc. for a total of \$9,940.00. The Federal Schedule C reported the following expenses:

Sports with clients	\$1,092
Telephone - alloc.	360
Accounting	150
Magazines, newspapers, etc.	396
Telephone - outside	192

Auto travel	
8,650 mi. @ 17¢	1,471
Tolls	108
Hospitality on weekends - dinners	1,236
Dry cleaning expense (47 days away)	496
Travel needs	141
Creative consultants expense	653
Photographic consultants	413
Outside services	<u>1,085</u>
Total	<u><u>\$7,998</u></u>

The \$7,998.00 in total expenses deducted from revenues of \$9,940.00 resulted in the \$1,942.00 net business income reported.

(ii) The wage and tax statements attached to the return showed \$55,857.58 from Sudler & Hennessey Incorporated and \$865.38 from Fischer Medical Publications, Inc., both of New York City, as "wages, tips, other compensation". Additionally, petitioner received a supplemental wage and tax statement from Sudler & Hennessey Incorporated in the amount of \$36.20 which indicated that said amount was not wages, but was group term life insurance. Each wage and tax statement was stamped with an arrow pointing to the amount contained in the "wages, tips, other compensation" box with the legend "Included in Schedule C".

(iii) The unincorporated business tax return shows the following: net profit and total income from business before New York modifications was \$1,942.00; from this amount was subtracted \$56,723.00 (this amount was noted as "FICA wages included in Schedule C"), resulting in total net loss from business of \$54,781.00.

(b) The 1979 return listed petitioners' occupations in the same manner as on the 1978 return. Virginia Trunk reported income of \$6,405.00 consisting of \$2,105.33 from Knock On Wood Natural Furniture, Inc. of Denville, New Jersey and \$4,300.00 from her htrnhand. petitioner DePaul Trunk. Since none

of her income was derived from New York sources, it was not reported on petitioners' 1979 New York State return. All references to "petitioner" shall, therefore, refer to DePaul Trunk only. Petitioner reported total income of \$58,212.00 consisting of \$52,432.00 wages, \$266.00 interest income, \$5,176.00 business income and \$338.00 other income. Petitioner claimed to have worked a total of 237 days for the year, 188 of which were worked in New York State. He, therefore, allocated approximately 79 percent of his wage income to New York State plus 100 percent of his business income of \$1,394.00 (the remaining \$3,782.00 represented the amount of Virginia Trunk's net profit from business as set forth on her Federal Schedule C) for a total of \$42,986.00. He then subtracted \$338.00, the amount reported for Federal purposes as other income, for a total New York income of \$42,648.00.

(i) The copy of petitioner's Federal Schedule C attached to the return indicated income from his business or profession as a marketing consultant consisting of \$14,999.00 from a percentage of consulting revenues and \$250.00 from consultations for a total of \$15,249.00. The Federal Schedule C reported the following expenses:

Sports with clients	\$ 637
Telephone - alloc.	360
Accounting	175
Magazines, newspapers, etc.	308
Telephone - outside	493
Auto travel	
8,890 miles @ 18½¢	1,644
Tolls	111
Hospitality on weekends, dinners	1,481
Dry cleaning expense (49 days away)	512
Travel needs	213
Creative consultants expense	846
Photography & photographic consultants	638
Outside services	937
Payments to marketing assistant	
Virginia Trunk	4,300
Secretarial A.M.	1,200

The \$13,855.00 in total expenses deducted from revenues of \$15,249.00 resulted in the \$1,394.00 net business income reported.

(ii) The wage and tax statements attached to the return showed \$67,430.69 from Sudler & Hennessey, Inc. of New York City. Additionally, petitioner received a wage and tax statement from Young & Rubicam of New York City in the amount of \$337.75 which indicated that said amount was not wages, but was the cost of group life insurance. The wage and tax statement from Sudler & Hennessey, Inc. was stamped with an arrow pointing to the amount contained in the "wages, tips, other compensation" box with the legend "Included in Schedule C" and the amount of \$14,999.00 which was circled and placed next to said legend.

(iii) The unincorporated business tax return shows the following: net profit and total income from business before New York modifications was \$1,394.00; from this amount was subtracted \$14,999.00 (this amount was noted as "FICA wages included in Schedule C"), resulting in total net **loss** from business of \$13,605.00.

2. Petitioners' tax returns were selected for examination along with those of approximately 100 other taxpayers on the basis that their 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 24, 1982, the Audit Division issued a Statement of Audit Changes to petitioners for the year 1978 which asserted additional New York State personal income tax and City of New York nonresident earnings tax due in the amount of \$771.94 plus interest. The basis was stated as follows:

"The expenses claimed in Schedule C are not ordinary and necessary in the production of income as an employee. Therefore, they have been disallowed."

On April 14, 1982, the Audit Division issued to petitioners a Notice of Deficiency for the year 1978 asserting additional tax due in the amount of \$771.94, plus interest of \$222.69, for a total amount due of \$994.63.

(b) On February 2, 1983, the Audit Division issued to petitioners a Statement of Audit Changes for the year 1979 asserting additional New York State personal income tax and City of New York nonresident earnings tax due in the amount of \$1,262.09 plus interest. The basis was stated as follows:

"As salaried employees, 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 employees."

Petitioners' medical expenses were adjusted to reflect increased income and their limitation percentage was recomputed to reflect income as reported on wage and tax statements. On April 8, 1983, the Audit Division issued to petitioners a Notice of Deficiency in the amount of \$1,262.09, plus interest of \$419.53, for a total amount due of \$1,681.62.

(c) For both of said years, petitioners itemized their deductions.

4. (a) Upon the submission, petitioners submitted documentary evidence and, in some cases, cancelled checks pertaining to the amounts claimed for sports with clients, telephone expenses, accounting, etc. No evidence was submitted to substantiate that these expenses were other than personal in nature.

(b) A letter to petitioner DePaul Trunk from Minturn V. Chace, Vice President and Treasurer of Sudler & Hennessey Incorporated, bearing the date of January 1, 1979, stated that a 1978 bonus check in the amount of \$9,075.00 was enclosed therewith. **An** undated letter from Steve Fischer, President of Fischer Medical Publications, Inc., stated that petitioner DePaul Trunk's compensation for 1977-1978 was based, pursuant to their agreement, on salary plus a planned percentage of the business to be determined annually. With the exception of those pertaining to life insurance, each of the wage and tax statements issued to petitioner DePaul Trunk by Sudler & Hennessey, Inc. and Fischer Medical Publications, Inc. for the years at issue provided for payroll deductions for Federal, State and local taxes and FICA. The wage and tax statements from Sudler & Hennessey, Inc. indicated that petitioner was a member of a company pension plan and further indicated that, for the year 1979, an amount was withheld for State **unemployment/disability**.

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 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 **or** capricious. The returns were patently erroneous and the Audit Division was justified in disallowing the claimed Schedule C business income.

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

C. That petitioner DePaul Trunk has not sustained his burden **of** proof under section 689(e) of the Tax Law and section U46-39.0(e) of the Administrative Code of the City of New York to show that he was engaged in a trade or business other than as an employee. Therefore, expenses claimed **on** Schedule C may not be deducted under section 62(1) of the Internal Revenue Code.


D. That, for the year 1978, petitioners have established that they were entitled to a Schedule A itemized deduction for the sum of \$150.00 paid to Albert **M.** Sasson for preparation of income tax returns.

E. That the petitions of DePaul Trunk and Virginia Trunk are granted to the extent indicated in Conclusion of Law "D", supra; that the Audit Division is directed to modify the Notice of Deficiency issued April 14, 1982 accordingly; and that, except as **so** granted, the petitions are in all other respects denied.

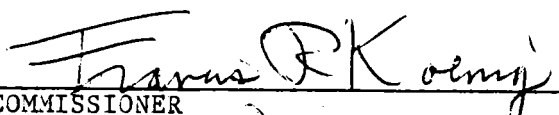
DATED: Albany, New York

STATE TAX COMMISSION

APR 17 1987



PRESIDENT



COMMISSIONER

