

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

JOHN SIDORICK AND BETTY SIDORICK

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 Nonresident Earnings Tax under Chapter 46, Title U of the Administrative Code of the City of New York for the Year 1978 and 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 1979.

Petitioners, John Sidorick and Betty Sidorick, 6040 Boulevard East, #18B, West New York, New Jersey 07093, 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 nonresident earnings tax under Chapter 46, Title U of the Administrative Code of the City of New York for the year 1978 and 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 1979 (File Nos. 38333 and 42913).

On October 23, 1985, petitioners waived their right to a formal hearing and requested the State Tax Commission to render a decision based on the entire record contained in the 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 petitioners have substantiated that they were engaged in a trade or business during the year at issue.

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

FINDINGS OF FACT

1. Petitioners, John Sidorick and Betty Sidorick, timely filed a New York State Income Tax Nonresident Return with City of New York Nonresident Earnings Tax for 1978 wherein they elected a filing status of "Married filing joint Return". Petitioner John Sidorick timely filed a New York State Income Tax Resident Return for the year 1979 wherein he elected a filing status of "Married filing separate returns (on separate **forms**)".

(a) **The 1978** New York State tax return listed Mr. Sidorick's occupation as repair service and inventor. Petitioners reported that their total New York income included business income of \$20,069.00.

(i) A copy **of** the Federal Schedule **C**, encaptioned Profit or **(Loss)** From Business or Profession showed "Revenues" of \$25,621.00 and the following listed expenses:

Tools	\$583.00
Travel	961.00
Materials-Lucite Steel Fabrication	986.00
Safety Equipment	149.00
Arctic Gear	186.00
Gloves	133.00
Design Magazines, Technical References	203.00
Hospitality	944.00
Veatinu Expenses	873 00

Drawing Board Supplies	281.00
Telephone Required by Employer (\$16x12)	192.00
Batteries	<u>62.00</u>
TOTAL	\$5,552.00

The \$5,552.00 in expenses deducted from revenues of \$25,621.00 resulted in the \$20,069.00 net business income reported.

(ii) The wage and tax statement attached to the return showed "Wages and other Compensation" of \$25,621.03 from New York Telephone Company. The statement was stamped with an arrow pointing to the \$25,621.03 figure with the legend "Included in Schedule C".

(iii) The New York State Unincorporated Business Tax Return reported a net profit and total income from business before New York modifications of \$20,069.00. The amount was reduced by \$25,621.00 resulting in a loss of \$5,552.00.

(b) The 1979 New York State Income Tax Resident Return listed Mr. Sidorick's occupation as repair service and inventor and reported total income of \$19,897.00 consisting of \$38.00 interest income and \$19,859.00 in business income.

(i) The Federal Schedule C reported "Revenues" of \$29,637.00 with the following expenses:

Tools	\$ 931.00
Travel (7,340 mi. @18½¢)	1,358.00
Materials-Lucite/Steel Fabrication	972.00
Safety Equipment	282.00
Artic Gear	303.00
Gloves	182.00
Design Magazines Technical Reference	347.00
Hospitality	986.00
Meeting expenses	974.00
Drawing Board Supplies	481.00
Telephone Required by Employer	192.00
Batteries	1 68 00

Photography	493.00
Testing Anti-Static & Anti-Spark Switches in Combustible Processes	1,174.00
Photo-Optic LIghting Testing in Combustible Processes	<u>\$ 935.00</u>
TOTAL	\$9,778.00

The \$9,778.00 in expenses deducted from revenues of \$29,637.00 resulted in the \$19,859.00 business income reported.

(ii) The wage and tax statement attached to the return showed \$28,587.10 in "Wages and other Compensation" from New York Telephone Company. The wage and tax statement was stamped with an arrow pointing to the \$28,587.10 figure with the legend "Included in Schedule C".

(iii) The New York State Unincorporated Business Tax Return reported a net profit of \$19,859.00 less subtractions of \$28,587.00 resulting in a net loss from the business of \$8,728.00.

(c) The New York State income tax return for 1978 claimed the standard deduction. However, Mr. Sidotick claimed a New York itemized deduction for 1979 in the amount of \$755.00 arising from taxes, interest and charitable contributions.

2. Petitioners' tax returns were selected for examination along with those of approximately 100 other individuals 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. On March 26, 1982, the Audit Division issued a Statement of Audit Changes to petitioners asserting a deficiency of New York State personal income ~~tax~~ for the year 1978 in the amount of \$632.17. The Audit Division also recomputed the New York City nonresident earnings tax which resulted in the conclusion that petitioner's had overstated the tax due by \$13.21. Consequently, the Audit Division concluded that there was a deficiency of \$618.96. The explanation for the proposed adjustment of New York State personal income tax was that "[b]usiness expenses claimed are not allowed as they are not considered ordinary and necessary in the production of income as a salaried employee." On July 9, 1982 the Audit Division issued a Notice of Deficiency to petitioners for said amount, plus interest.

4. On February 8, 1983, the Audit Division issued a Statement of Audit Changes to Mr. Sidorick asserting a deficiency for 1979 of \$1,052.98 in New York State personal income tax and \$330.72 in New York City personal income tax. The Statement of Audit Changes explained that "[a]s a salaried employee, YOU are not a business entity and therefore not entitled to claim Schedule C deductions as these expenses are not ordinary and necessary for the production of income as an employee." On April 8, 1983, the Audit Division issued a Notice of Deficiency to petitioner for said amount, plus interest.

5. Petitioners submitted documentary evidence consisting of, inter alia, sales invoices, cancelled checks and worksheets in substantiation of a portion of the business expenses claimed on Mr. Sidorick's Federal Schedule C. However, the evidence submitted is insufficient to establish (i) that Mr. Sidorick was engaged in the carrying on of a trade or business.

(ii) that the expenses constituted employee trade *or* business deductions pursuant to Internal Revenue Code § 62(2); and (iii) that the expenses constituted ordinary and necessary business expenses and not personal expenditures.

6. Petitioners contend:

(a) That the Notice of Deficiency was 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 petitioner is 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 petitioner does not have cancelled checks or other receipts for certain expenses, the Department of Taxation and Finance should allow petitioner a reasonable estimate *of* such expenses.

CONCLUSIONS OF LAW

A. That section 683(a) *of* the Tax law provides that tax shall be assessed within three years after the return was filed regardless of whether the return was filed on or after the date prescribed. Section 683(b)(1) of the Tax Law provides, in general, that an income tax return filed before the last date prescribed shall be deemed filed on such last day. Since the Notice of Deficiency dated July 9, 1982 was not issued within three years of the date the tax return for 1978 was deemed filed, the Notice of Deficiency asserting Tax Due for the year 1978 was barred by the statute of limitations.

B. That the Notice of Deficiency, dated April 8, 1983, was properly issued and was not arbitrary and capricious. The return was patently erroneous and the Audit Division was justified in disallowing the business expenses.

claimed by Mr. Sidorick **on** his Federal Schedule C. The Notice of Deficiency was preceded by a Statement of Audit Changes and petitioners had an opportunity to file an amended return claiming employee business expenses as adjustments on Federal **Form** 2106, or as itemized miscellaneous deductions, but did not do **so**.

C. 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.

D. That petitioners have failed to sustain their burden of proof (Tax Law § 689[e]; Administrative Code §§ T46-189.0[e]) to show **(i)** that **Mr.** Sidorick 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).

E. That the petition **of** John Sidorick and Betty Sidorick is granted to the extent **of** Conclusion **of** Law "A" and the Notice of Deficiency dated July 9, 1982 **is** cancelled; except as **so** granted, the petition is **in** all other respects denied and the Notice of Deficiency dated April 8, 1982 **is** sustained **in** full, together with such additional interest as may be lawfully due and owing.

DATED: Albany, New York

STATE TAX COMMISSION

JUN 18 1987

PRESIDENT


COMMISSIONER

COMMISSIONER