

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

EDWARD NORMAN

DECISION

for Redetermination of a Deficiency or for
Refund of Personal Income Tax and Unincorporated :
Business Tax under Articles 22 and 23 of the
Tax Law for the Years 1978 through 1981.

Petitioner, Edward Norman, 903 Military Road, Kenmore, New York 14217,
filed a petition for redetermination of a deficiency or for refund of personal
income tax and unincorporated business tax under Articles 22 and 23 of the Tax
Law for the years 1978 through 1981 (File No. 48468).

A hearing was held before Brian L. Friedman, Hearing Officer, at the
offices of the State Tax Commission, 65 Court Street, Buffalo, New York, on
September 15, 1986 at 2:45 P.M., with all briefs to be submitted by December 1,
1986. Petitioner appeared by Frank Ostrowski. The Audit Division appeared by
John P. Dugan, Esq, (Deborah J. Dwyer, Esq., of counsel).

ISSUE

Whether, based upon a source and application of funds audit and an examination
of available books and records, the Audit Division properly found additional
funds subject to personal income tax and unincorporated business tax.

FINDINGS OF FACT

1. For each of the years 1978 through 1980, Edward Norman (hereinafter
"petitioner") timely filed a joint New York State Income Tax Resident Return
with his wife, Stephanie, who died on November 26, 1980. For the year 1981,

petitioner timely filed a New York State Income Tax Return for the year 1981.

of the years 1978 through 1980, petitioner timely filed a New York State Unincorporated Business Tax Return.

2. On January 15, 1982 and on January 26, 1983, petitioner executed consents fixing periods of limitation upon assessment of personal income and unincorporated business taxes, agreeing that personal income taxes and unincorporated business taxes for the taxable years ending December 31, 1978 and December 31, 1979 could be assessed at any time on or before April 15, 1984.

3. On July 19, 1983, the Audit Division issued to petitioner a Statement of Personal Income Tax Audit Changes which advised him that, as a result of a source and application of funds analysis, additional personal income tax was due in the amounts of \$303.65 for 1978, \$542.02 for 1979, \$1,492.96 for 1980 and \$1,312.00 for 1981. Also on July 19, 1983, the Audit Division issued to petitioner a Statement of Unincorporated Business Tax Audit Changes which advised him that, as a result of the personal income tax audit and additional New York State lottery sales for 1978 and 1980, additional unincorporated business tax was due in the amounts of \$257.10 for 1978, \$332.42 for 1979 and \$586.99 for 1980. Accordingly, on September 1, 1983, the Audit Division issued to petitioner three notices of deficiency as follows:

<u>Period</u>	<u>Additional Tax</u>	<u>Penalty</u>	<u>Interest</u>	<u>Total Amount Due</u>
1978, 1979, 1980	\$2,338.63	\$116.93	\$759.06	\$3,214.62
1978, 1979, 1980	1,176.51	58.83	404.67	1,640.01
1981	1,312.00	65.60	211.72	1,589.32

4. For the years at issue, petitioner operated, as a sole proprietorship, a bar and restaurant known as the Mark IV at 903 Military Road, Kenmore, New York. Petitioner also resided at this address. A detailed field audit was performed in which petitioner's books and records, including cash receipts, bank statements and cancelled checks

expenditures and to determine the sources of funds being deposited into the business checking accounts, as well as into his personal checking account and savings accounts. From an examination of petitioner's books and records, the auditor determined that said books and records were inadequate to properly account for the expenses and receipts. The auditor resorted, therefore, to an indirect method of income reconstruction, a source and application of funds analysis. The results of this analysis were as follows:

	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
Sources of Funds	\$18,147.78	\$20,258.45	\$36,011.12	\$45,947.
Applications of Funds	<u>23,277.37</u>	<u>27,678.64</u>	<u>54,312.20</u>	<u>72,319.</u>
Excess of applications over sources	\$ 5,129.59	\$ 7,420.19	\$18,301.08	\$26,372.

5. At a pre-hearing conference, petitioner's representative submitted information which resulted in the following adjustments:

<u>Sources</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
Prior to conference	\$18,147.78	\$20,258.45	\$36,011.12	\$45,947.09
Insurance proceeds	--	--	3,048.66	(3,048.66)
Estate proceeds	--	--	--	4,200.00
Depreciation	--	--	--	175.00
Tax Refunds	--	257.00	--	--
Total sources	<u>\$18,147.78</u>	<u>\$20,515.45</u>	<u>\$39,059.78</u>	<u>\$47,273.43</u>
<u>Applications</u>				
Prior to conference	\$23,277.37	\$27,678.64	\$54,312.20	\$72,319.44
Food (wife deceased)	--	--	(80.00)	(750.00)
Clothing	(150.00)	(150.00)	(200.00)	(200.00)
Auto	(300.00)	(300.00)	(300.00)	(300.00)
Total applications	<u>\$22,827.37</u>	<u>\$27,228.64</u>	<u>\$53,732.20</u>	<u>\$71,069.44</u>
Excess of applications over sources	\$ 4,679.59	\$ 6,713.19	\$14,672.42	\$23,796.01

As a result of the above adjustments, additional tax due was recomputed as follows:

Additional personal income tax due	\$271.86	\$476.69	\$1,026.39	\$1,023.;
Additional unincorporated business tax due	234.63	300.63	451.08	--

6. Petitioner's sole contention with regard to the accuracy of the source and application of funds analysis **is** that the Audit Division failed to properly credit petitioner with cash on hand at the beginning of the audit period. Cash on hand was estimated at \$1,000.00 for each of the years 1978, 1979 and 1980 and \$1,250.00 for 1981. Petitioner contends that, **in** years prior to the audit (1967 through 1977), he had reported capital gain **of** \$9,161.00, interest income of \$12,562.00 and nontaxable income of \$87,000.00. The Audit Division determined, however, that, for the years 1975 through 1981, petitioner had purchased assets and had made capital improvements totalling in excess of \$80,000.00. Petitioner further contends that two deposits to his checking account **on** January 4, 1982, totalling \$7,827.08, were improperly credited for **the year** 1981 and, therefore, added to his income for 1981. The auditor stated that **it is** the usual audit practice that the first or second deposits made in a calendar year are considered to be deposits in transit and are, therefore, treated as receipts for the prior year. The auditor admitted that the two deposits, totalling \$7,827.08, made on January 4, 1982, were determined to be deposits for the year 1981, but stated that, at the beginning of the audit period (January 1, 1978), deposits totalling \$12,698.81, made on January 3, 1978, were also considered **to be** deposits in transit and were, therefore, considered to be deposits in the year 1977, thereby increasing petitioner's balance at the beginning of the audit period. Petitioner further alleges that a considerable amount of cash on hand was kept at his residence. No evidence was introduced at the hearing held herein to substantiate this allegation.

CONCLUSIONS OF LAW

A. That, pursuant to the provisions of sections 689(e) and 722(a) of **the Tax Law**, petitioner bears the burden of proof to establish that

income tax and unincorporated business tax deficiencies asserted herein.

Petitioner's allegations that, in the performance of its source and application of funds analysis, the Audit Division erred in its estimate of petitioner's cash on hand were not supported by credible evidence.


B. That the petition of Edward Norman is granted only to the extent indicated in Finding of Fact "5"; that the Audit Division is directed to modify the notices of deficiency issued September 1, 1983 accordingly; and that, except as so granted, the petition is in all other respects denied.

DATED: Albany, New York

STATE TAX COMMISSION

FEB 10 1987


PRESIDENT


COMMISSIONER


COMMISSIONER