

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

NICHOLAS PAVLOU and CHRISTINA PAVLOU

DECISION

for Redetermination **of** a Deficiency or for
Refund of Personal Income Tax under Article 22
of the Tax Law for the Years 1979, 1980 and
1981.

Petitioners Nicholas Pavlou and Christina Pavlou, 623 Bellevue Avenue
North, Yonkers, New York 10703, filed a petition for redetermination of **a**
deficiency or for refund of personal income tax under Article 22 of the Tax Law
for the years 1979, 1980 and 1981 (File Nos. 51758 and 51759).

A hearing was held before Allen Caplowaith, Hearing Officer, at the
offices **of** the State Tax Commission, Two World Trade Center, New York, New
York, **on** December 17, 1985 at 9:15 A.M. Petitioner appeared by James Kotiadis
and Socrates Scott L. Nicholas. The Audit Division appeared by John P. Dugan,
Esq. (Herbert Kamrass, Esq., of counsel).

ISSUES

I. Whether the Audit Division properly attributed additional personal
income to petitioners in the form of constructive dividends based on a sales
tax audit of a corporation of which petitioners were the sole shareholders.

11. Whether certain adjustments made as the result of an income tax field
audit were proper.

FINDINGS OF FACT

1. Petitioners, Nicholas & Christina Pavlou, filed a New York State
Income Tax Resident Return for each **of** the years 1979 and 1980 under filing

status "married filing separately on one return". For 1981, they filed their return under filing status "married filing joint return".

2. On October 31, 1983, the Audit Division issued a separate Statement of Personal Income Tax Audit Changes to each petitioner based, in part, on the results of a sales tax audit conducted for the periods December 1, 1978 through August 31, 1981. Said statements incorporated the following adjustments:

- To Nicholas Pavlou	<u>1979</u>	<u>1980</u>	<u>1981</u>
Constructive Dividends from Nicks over-Leaf Deli, Inc.	\$24,561.64	\$23,788.64	\$ 8,086.
able Capital Gain			1,740.
-2 addition - Capital Gain			435.
iveness of Corporated (sic) Debt			34,184.
Debt Disallowed \$40,000.00			
tal Loss Disallowed		1,500.00	
tal Loss Carryover Disallowed			1,500.
cal Adjustment Due to Change in AGI	620.87		
rest Income Reallocated	1,503.64		
ption Reallocated		750.00	
Return Converted to Separate Returns			
located Taxable Income			(6,514.
dard Deduction			(500.
Adjustment	<u>\$26,686.15</u>	<u>\$26,038.64</u>	<u>\$38,932.</u>
- To Christina Pavlou	<u>1979</u>	<u>1980</u>	<u>1981</u>
Constructive Dividends from Nicks over-Leaf Deli, Inc.	\$24,561.63	\$23,788.64	\$ 8,086.
ble Capital Gain			1,740.
2 Addition - Capital Gain			435.
Debt Disallowed \$40,000.00			
tal Loss Disallowed		1,500.00	
tal Loss Carryover Disallowed			1,500.
cal Adjustment Due to Change in AGI	620.86		
rest Income Reallocated	(1,503.64)		
ption Reallocated		(750.00)	
Return Converted from Joint to			
married Filing Separate			
Located Taxable Income			(7,922.
Adjustment	<u>\$23,678.85</u>	<u>\$24,538.64</u>	<u>\$ 3,840.</u>

3. Based on the aforestated adjustments, four (4) notices of deficiency were issued against petitioners on February 2, 1984 as follows:

- a - against Nicholas Pavlou, asserting additional personal income tax of \$5,910.95 for the years 1979 and 1980, penalty of \$295.55, plus interest of \$2,301.29, for a total due of \$8,507.79.
- b - against Nicholas Pavlou, asserting additional personal income tax of \$4,010.51 for the year 1981, penalty of \$200.52, plus interest of \$853.15, for a total due of \$5,064.18.
- c - against Christina Pavlou, asserting additional personal income tax of \$5,304.66 for the years 1979 and 1980, penalty of \$265.24, plus interest of \$2,058.30, for a total due of \$7,628.20.
- d - against Christina Pavlou, asserting additional personal income tax of \$113.61 for the year 1981, penalty of \$5.68, plus interest of \$24.16, for a total due of \$143.45.

All of the aforesated penalties were asserted for negligence pursuant to section 685(b) of the Tax Law.

4. On February 16, 1983, petitioners executed a consent form extending the period of limitation on assessment for the taxable year ended December 31, 1979 to any time on or before April 15, 1984.

5. During the years at issue petitioners were officers and the sole shareholders of Nick's Clover-Leaf Delicatessen, Inc. ("the Corporation").

6. The corporation's premises were destroyed by fire on July 24, 1981. All books and records were destroyed in the fire except the general ledger, a copy of the 1980 federal income tax return, and copies of sales tax returns, forms ST-100, which were in the custody of petitioners' accountant, Mr. Robert Hochhauser.

7. Since inadequate records were available, taxable ratio and markup tests could not be performed for the sales tax audit.

8. On July 29, 1981, petitioners' accountant submitted a schedule of the Corporation's sales figures for the months of January through June 1981.

aforesaid fire. The sales figures reported thereon were specific odd amounts. Nothing in the schedule indicated that the sales figures were estimated.

9. The sales figures reported in the aforesaid schedule were 21.958% greater than those reported on the sales tax returns. Accordingly, reported sales for the entire audit period were increased by said percentage, yielding audited gross sales of \$714,850.72. Reported gross sales were \$586,145.00. Applying a taxable ratio **of** 37.46% yielded an amount for additional sales tax due for the audit period of \$6,902.40, which was consented to and paid by the petitioners.

10. Since inadequate records were available for the performance of an income tax audit, the additional gross sales per the sales tax audit were attributed to petitioners as additional income in the nature of constructive dividends from the Corporation, which were divided equally between petitioners for each of the years at issue.

11. Although petitioners consented to the sales tax assessed, they now contend that the sales reported **on** the forms ST-100 were accurate and that the sales reported in the aforesaid letter from their accountant were estimated. To support such contention, petitioners submitted an affidavit, sworn to by Mr. Hochhauser on June 25, 1985, wherein he stated that the sales figures he previously reported in his letter of July 29, 1981 "were derived from memory and intended only to be estimates",

12. The record indicates that the Corporation made loans to petitioner Nicholas Pavlou. The balance of said loans outstanding appeared on the Corporation's balance sheet as an asset **of** \$34,184.00 as of December 31, 1980. The balance sheet for December 31, 1981 showed no such loans. Accordingly, **the**

Audit Division determined that the corporation forgave the debt, thereby creating taxable income in said amount to **Mr.** Pavlou.

13. Although petitioners alleged that no such loans existed and the balance sheet reporting of such loans represented an accounting error, no credible evidence was submitted to support such allegation.

14. A long term capital **loss** attributable to a bad debt of \$40,000.00 was claimed on petitioners' 1980 tax return and disallowed for lack of substantiation. The related 1980 capital **loss** deduction of \$3,000.00 and 1981 loss carryover deduction of \$3,000.00 resulting from such claimed bad debt were also disallowed. Although petitioner Christina Pavlou claimed the bad debt arose from loans to her brother, whose business subsequently went bankrupt making such debt worthless, no evidence was submitted to show that a bona fide debt existed; that funds were actually transferred **to** her brother from petitioners' accounts; or that petitioner had the funds available to make such loan.

15. Petitioners' 1981 return was changed by the Audit Division from a joint return to separate returns. The resulting recomputation was to the benefit of petitioners and the adjustments made with respect to such change of filing status were not contested.

CONCLUSIONS OF LAW

A. That where there is some factual basis for deciding that the tax return as filed does not accurately reflect the true income received by a taxpayer, the Audit Division may determine proper income using indirect methods (see Holland v. United States, 348 U.S. 121, 131-132). The sales **tax** audit conducted by the Audit Division revealed \$6,902.40 in sales tax due. **Such** determination provided a factual basis for deciding **that the** income reported by petitioners **on their income tax returns was not accurate and that the income reported**

used the sales tax audit findings in its calculation of income tax. Nowhere in the Tax Law or regulations is the Audit Division precluded from utilizing the results of an audit conducted under one article of the Tax Law in an audit conducted under another article.


B. That petitioners have failed to sustain their burden of proof, imposed pursuant to section 689(e) of the Tax Law, to show that they are properly entitled to a bad debt deduction or that the adjustment made with respect to the forgiveness of loans by the corporation was erroneous or improper. According to the adjustments made with respect to the bad debt deduction and the forgiveness of loans are sustained.

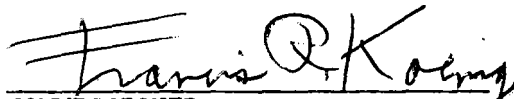
C. That the petition of Nicholas Pavlou and Christina Pavlou is denied and the notices of deficiency issued February 2, 1984 are sustained together with such additional penalty and interest as may be lawfully owing.


DATED: Albany, New York

STATE TAX COMMISSION

APR 28 1986


PRESIDENT


COMMISSIONER


COMMISSIONER