

Page 2

Affidavit of Mailing

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this
14th day of March, 1985.

David Parbruch

James O'Donoghue
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Cargain Service Station, Inc. :

for Redetermination of a Deficiency or for Refund :
of Corporation Franchise Tax under Article 9A of :
the Tax Law for the Fiscal Years Ended 9/30/77 & :
9/30/78. :

In the Matter of the Petition :
of :
Richard and Nancy Cargain :

for Redetermination of a Deficiency or for Refund :
of Personal Income Tax under Article 22 of the Tax :
Law for the Years 1977 and 1978. :

AFFIDAVIT OF MAILING

In the Matter of the Petition :
of :
George Cargain :

for Redetermination of a Deficiency or for Refund :
of Personal Income Tax under Article 22 of the Tax :
Law for the Years 1977 and 1978. :

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 14th day of March, 1985, he served the within notice of Decision by certified mail upon Cargain Service Station, Inc., the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Cargain Service Station, Inc.
Route 6
Mahopac, NY 10541

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

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14th day of March, 1985.

David Parachuck

Constance A. Hayward
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

March 14, 1985

Cargain Service Station, Inc.
Route 6
Mahopac, NY 10541

Gentlemen:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1090 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Wolf Magalnick
Old Stone Bldg., P.O. Box 603
Mahopac, NY 10541
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Cargain Service Station, Inc. :
for Redetermination of a Deficiency or for Refund :
of Corporation Franchise Tax under Article 9A of :
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George Cargain
Rt. 6N - Mahopac Falls
Mahopac, NY 10541

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Bonnie A. Hendon
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pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

March 14, 1985

George Cargain
Rt. 6N - Mahopac Falls
Mahopac, NY 10541

Dear Mr. Cargain:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 690 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

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Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
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Cargain Service Station, Inc. :

for Redetermination of a Deficiency or for Refund :
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In the Matter of the Petition :
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Richard and Nancy Cargain :

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Law for the Years 1977 and 1978. :

AFFIDAVIT OF MAILING

In the Matter of the Petition :
of :
George Cargain :

for Redetermination of a Deficiency or for Refund :
of Personal Income Tax under Article 22 of the Tax :
Law for the Years 1977 and 1978. :

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 14th day of March, 1985, he served the within notice of Decision by certified mail upon Richard & Nancy Cargain, the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Richard & Nancy Cargain
Union Valley Rd.
Mahopac, NY 10541

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

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14th day of March, 1985.

David Parcluck

James P. O'Connell
Authorized to administer oaths
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STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

March 14, 1985

Richard & Nancy Cargain
Union Valley Rd.
Mahopac, NY 10541

Dear Mr. & Mrs. Cargain:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 690 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

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STATE TAX COMMISSION

cc: Petitioner's Representative
Wolf Magalnick
Old Stone Bldg., P.O. Box 603
Mahopac, NY 10541
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
CARGAIN SERVICE STATION, INC. : DECISION
for Redetermination of a Deficiency or for :
Refund of Corporation Franchise Tax under :
Article 9-A of the Tax Law for the Fiscal Years :
Ended September 30, 1977 and September 30, 1978. :
:

In the Matter of the Petition :
of :
RICHARD and NANCY CARGAIN :
for Redetermination of a Deficiency or for :
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Years 1977 and 1978. :

In the Matter of the Petition :
of :
GEORGE CARGAIN :
for Redetermination of a Deficiency or for :
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Years 1977 and 1978. :
:

Petitioner Cargain Service Station, Inc., Route 6, Mahopac, New York 10541, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the fiscal years ended September 30, 1977 and September 30, 1978 (File No. 39064).

Petitioners Richard and Nancy Cargain, Union Valley Road, Mahopac, New York 10541, 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 1977 and 1978 (File Nos. 39223 and 39224).

Petitioner George Cargain, Route 6N-Mahopac Falls, Mahopac, New York 10541, 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 1977 and 1978 (File No. 39187).

A consolidated formal hearing was held before Frank W. Barrie, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on May 9, 1984 at 9:15 A.M., with all briefs to be submitted by July 13, 1984. All of the petitioners appeared by Wolf Magalnick, C.P.A. The Audit Division appeared by John P. Dugan, Esq. (Kevin A. Cahill, Esq., of counsel).

ISSUES

Whether the income reconstruction audits of petitioners Richard and Nancy Cargain and petitioner George Cargain properly reflected their respective income and whether additional income was properly attributed to petitioner Cargain Service Station, Inc.

FINDINGS OF FACT

1. On September 1, 1981, the Audit Division issued a Statement of Franchise Tax Audit Changes against petitioner Cargain Service Station, Inc. alleging corporation franchise tax due of \$2,111.20 plus interest and \$2,348.40 plus interest for the fiscal years ended September 30, 1977 and September 30, 1978, respectively. Such audit changes were based on a determination by the Audit Division that the service station had unreported additional gross receipts of \$21,720.00 and \$23,484.00 for the fiscal years ended September 30, 1977 and September 30, 1978, respectively.

2. On September 1, 1981, the Audit Division also issued a Statement of Personal Income Tax Audit Changes against petitioner George Cargain alleging

additional income tax due of \$684.18 plus interest and \$906.10 plus interest for 1977 and 1978, respectively. The Audit Division explained in such statement that the taxes alleged due were based on a field audit which determined that Cargain Service Station, Inc. had additional income in the amount noted in Finding of Fact "1", supra. One-half of such income was allocated to petitioner George Cargain, the corporation's president, and the other half to petitioner Richard Cargain, the corporation's secretary. As a result, the Audit Division attributed additional income of \$10,860.00 and \$11,742.00 to petitioner George Cargain for 1977 and 1978, respectively.

3. On September 1, 1981, the Audit Division issued a Statement of Personal Income Tax Audit Changes against petitioners Richard and Nancy Cargain¹ alleging additional income tax due of \$750.93 plus interest and \$958.28 plus interest for 1977 and 1978, respectively. The Audit Division explained in such statement that the taxes alleged due were based on a field audit which determined that Cargain Service Station, Inc. had additional income. One-half of such income, \$10,860.00 for 1977 and \$11,742.00 for 1978, was allocated to petitioners Richard and Nancy Cargain.

4. On April 30, 1982, the Audit Division issued two Notices of Deficiency against petitioner Cargain Service Station, Inc. alleging corporate tax deficiencies of \$2,111.20 plus interest and \$2,348.40 plus interest for the fiscal years ended September 30, 1977 and September 30, 1978, respectively. The Notice for the earlier year was not untimely because on September 12, 1981, petitioner Richard Cargain, as an officer of the corporate petitioner, had executed a

1 Petitioner Nancy Cargain is a party hereto for the sole reason that she is the wife of petitioner Richard Cargain.

consent which extended the period of limitation for the assessment of corporate tax for the fiscal year ended September 30, 1977 until November 8, 1982.

5. On April 14, 1982, the Audit Division issued a Notice of Deficiency against petitioner George Cargain alleging additional income tax due of \$1,590.28 plus interest for 1977 and 1978. The Notice was not untimely for the first year at issue because on September 12, 1981, petitioner George Cargain by his representative had executed a consent which extended the period of limitation for the assessment of 1977 income tax until November 8, 1982.

6. On April 14, 1982, the Audit Division issued two Notices of Deficiency against petitioners Richard and Nancy Cargain alleging additional income tax due of \$750.93 plus interest for 1977 and \$958.28 plus interest for 1978, respectively. The Notice for 1977 was not untimely because on September 12, 1981, petitioners Richard and Nancy Cargain by their representative had executed a consent which extended the period of limitation for the assessment of 1977 income tax until November 8, 1982.

6. Petitioner Cargain Service Station, Inc. filed corporation franchise tax reports for each of the fiscal years at issue and reported the following relevant information:

	<u>Fiscal Year Ended September 30, 1977</u>	<u>Fiscal Year Ended September 30, 1978</u>
Gross receipts	\$445,079.61	\$618,795.51
Less: Cost of goods sold	368,173.41	538,825.67
Gross profit	<u>\$ 76,906.20</u>	<u>\$ 79,969.84</u>
 <u>Deductions:</u>		
Compensation of officers	\$ 13,720.00	\$ 14,560.00
Salaries and wages	18,090.00	18,089.00
Repairs	436.98	433.92
Rents	20,000.00	21,625.00
Taxes	2,725.90	3,097.74
Depreciation	139.34	418.03

Pension plans	5,000.00	4,540.09
Advertising	-0-	337.50
Interest	-0-	40.00
Other deductions (including insurance, professional fees, telephone)	15,201.95 ²	14,359.56
Total Deductions	<u>\$ 75,319.17²</u>	<u>\$ 77,500.84</u>
Taxable Income	\$ 1,592.03	\$ 2,469.00

The corporation paid the minimum corporate tax of \$250.00 for the year ended September 30, 1977 and corporate tax of \$271.90 for the year ended September 30, 1978.

7. Petitioner George Cargain filed separately on the same New York income tax return with his wife, Elizabeth Cargain, for each of the years at issue. They reported "Total Income" for 1977 of \$10,729.63, of which \$9,066.31 was allocated to petitioner George Cargain and \$1,663.32 to Elizabeth Cargain. They reported "Total Income" for 1978 of \$13,225.18, of which \$11,461.15 was allocated to petitioner George Cargain and \$1,764.03 to Elizabeth Cargain.

8. Petitioners Richard and Nancy Cargain filed a joint New York State Income Tax Resident Return for 1977 on which they reported "Total Income" of \$9,439.28. They filed separately on the same tax return for 1978 and reported "Total Income" of \$12,273.38, of which \$11,206.44 was allocated to petitioner Richard Cargain and \$1,066.94 to Nancy Cargain.

9. Petitioner Cargain Service Station, Inc. was owned and operated by petitioners George Cargain and Richard Cargain. According to the audit report of the service station, it was a Mobil Station which had one island for gas pumps and three bays for repairs.

2 The tax return incorrectly noted the amount for total deductions as \$75,314.17.

10. Although petitioners' representative was not provided with all the audit workpapers and schedules prior to the hearing herein, he was given copies of the pertinent workpapers concerning the cash availability analysis performed by the Audit Division on the petitioners, Richard and Nancy Cargain and on petitioner George Cargain. In addition, petitioner's representative was given an adequate amount of time at the hearing to review the audit workpapers and schedules, which he had not seen prior to the hearing.

11. The Audit Division reconstructed the income of petitioners Richard and Nancy Cargain by a cash availability audit using a source and application of funds analysis which found the following:

<u>Sources</u>	<u>1977</u>	<u>1978</u>
Net salary	\$ 4,900.00	\$ 6,500.00
State tax refund	41.00	16.00
Federal tax refund	-0-	-0-
Total available	<u>\$ 4,941.00</u>	<u>\$ 6,516.00</u>
 <u>Applications</u>		
Deposits to checking account	\$ 2,290.00	\$ 4,048.00
Less transfers	(472.00)	(410.00)
Deposits to savings accounts	1,500.00 ⁴	1,828.00
Less transfers	-0-	-0-
Cash living expenses	<u>12,483.00</u>	<u>12,792.00</u>

3 The Audit Division properly subtracted out amounts deposited in petitioners' checking account which were transfers from their savings accounts because such amounts would have been included previously as "deposits to savings account."

4 This is an estimated amount because according to the audit papers, information concerning deposits to petitioners' Mahopac National Bank account #55514596 was "missing 1-1-77 to 12-31-77." Petitioners at the hearing herein introduced copies of the pages from the bank book for such account for 1977 (petitioners' Exhibit "2"). It shows deposits totalling \$4,434.98, an amount greatly in excess of the estimated \$1,500.00. Therefore, petitioners' total applications should have been substantially greater than the amount determined by the Audit Division (which would have resulted in a larger deficiency than the one alleged by the Audit Division against petitioners).

Total applications	15,801.00	18,258.00
Total sources	4,941.00	6,516.00
Difference to be explained	<u>\$10,860.00</u>	<u>\$11,742.00</u>

12. The cash living expenses of \$12,483.00 for 1977 and \$12,792.00 for 1978, as noted in Finding of Fact "11", supra, were calculated as follows by the Audit Division:

	1977		1977	
	by check	by cash	by check	by cash
Food	\$ -0-	\$4,160	\$ -0-	\$4,160
Clothing	167	-0-	402	-0-
Beauty and barber	-0-	300	-0-	300
Recreation and out of pocket	-0-	1,040	-0-	1,040
Mortgage	-0-	-0-	-0-	-0-
Insurance: Life	-0-	250	253	-0-
Home	-0-	320	322	-0-
Car	202	-0-	201	-0-
Real estate taxes:				
Town and County	-0-	1,010	-0-	1,030
School	-0-	1,300	-0-	1,350
Utilities	1,241	-0-	1,560	-0-
Medical	548	-0-	133	-0-
Home repairs	-0-	500	67	500
Gifts and allowances	-0-	200	-0-	200
Car payments	-0-	-0-	923	-0-
Miscellaneous	125	-0-	136	-0-
Dishwasher purchased	-0-	460	-0-	-0-
Additional based on consistent drawings of both brothers		\$ 4,392		\$ 5,112
Total		<u>\$13,932</u>		<u>\$13,692</u>
Less living expenses paid by savings withdrawals		1,449		900
		<u>\$12,483</u>		<u>\$12,792</u>

13. The Audit Division also reconstructed the income of petitioner George Cargain by a cash availability audit using a source and application of funds analysis which found the following:

Sources	1977	1978
Net salary	\$ 4,900.00	\$ 6,500.00
State tax refund	108.00	34.00
Federal tax refund	-0-	1,124.00
Total available	<u>\$ 5,008.00</u>	<u>\$ 7,658.00</u>

<u>Applications</u>		
Deposits to checking account	\$ 5,886.00	\$ 8,561.00
Less transfers	(250.00)	-0-
Deposits to savings	795.00	27,676.96
Less transfers	(85.00)	(26,483.96)
Cash living expenses	9,522.00	9,646.00
Total Applications	<u>\$15,868.00</u>	<u>\$19,400.00</u>
Total Sources	5,008.00 ⁵	\$ 7,658.00
Difference to be explained	<u>\$10,860.00</u>	<u>\$11,742.00</u>

14. The cash living expenses of \$9,522.00 for 1977 and \$9,646.00 for 1978, as noted in Finding of Fact "12", supra, were calculated as follows by the Audit Division:

	<u>1977</u>		<u>1978</u>
	<u>by check</u>	<u>by cash</u>	<u>by cash</u>
Food	\$ 548	\$ 5,692	\$ 5,100
Clothing	705	-0-	-0-
Barber and beauty	-0-	300	300
Recreation and out of pocket	-0-	1,040	1,040
Insurance: Life	361	-0-	-0-
Home	-0-	200	200
Mortgage Payments 150/month	-0-	1,800	1,800
Real estate taxes:			
Town & county	-0-	712	731
School	-0-	900	950
Medical	193	-0-	-0-
Miscellaneous	949	-0-	-0-
Unidentified	1,479	-0-	-0-
Gifts and allowances	-0-	300	300
Utilities	1,140	-0-	-0-
Total	5,375	10,944	11,021
Allowed paid by savings withdrawals		1,422	1,375
Cash living expenses		<u>\$ 9,522</u>	<u>\$ 9,646</u>

15. The Audit Division then determined that the petitioner service station had additional receipts of \$21,720.00 and \$23,484.00 for the fiscal years ended

5 There is nothing in the record that explains why the amounts representing the "difference to be explained" were the same amounts for both petitioner George Cargain and petitioners Richard and Nancy Cargain for each of the years at issue. It is a remarkable coincidence in light of the fact that the Audit Division conducted separate and detailed audits of the finances of petitioner George Cargain and petitioners Richard and Nancy Cargain.

September 30, 1977 and September 30, 1978, respectively by adding together the overapplication of funds determined in Findings of Fact "11" and "12" supra:

	FYE <u>9/30/77</u>	FYE <u>9/30/78</u>
Additional gross receipts		
George Cargain	\$10,860	\$11,742
Richard Cargain	<u>10,860</u>	<u>11,742</u>
Total additional receipts	<u>\$21,720</u>	<u>\$23,484</u>

16. None of the petitioners were present at the hearing to testify in support of their petitions. According to their representative, "They could not be here today in that they are all working." At the hearing, petitioners introduced the following evidence in support of their petitions:

- (1) A general statement allegedly signed by the father of petitioners George Cargain and Richard Cargain that he and his wife contributed between \$450 and \$475 per month to his sons "to help with food and shelter;"
- (2) An unsigned typewritten promissory note from Emerson Hyatt to Richard Cargain for which no adequate foundation or explanation was provided;
- (3) Copies of pages from a bankbook which, as noted in Footnote "4" of Finding of Fact "11", does not further the case of petitioners Richard and Nancy Cargain;
- (4) A general statement allegedly signed by William Coyle that he lived with his brother-in-law petitioner George Cargain during the years at issue and contributed \$50.00 and \$75.00 per week for food and rent;
- (5) An unsigned promissory note from Harold Coyle to George Cargain for which no adequate foundation or explanation was provided.

After the hearing, petitioners submitted two affidavits sworn to by petitioner George Cargain and petitioner Nancy L. Cargain.

CONCLUSIONS OF LAW

A. That pursuant to Tax Law section 689(e), the burden of proof is imposed upon petitioner George Cargain and petitioners Richard and Nancy Cargain to show that the audit method used by the Audit Division in reconstructing their income for 1977 and 1978 was inaccurate and/or incorrect. Likewise, pursuant to Tax Law section 1089(e), the burden of proof is upon the corporate petitioner to show that the Audit Division incorrectly determined that it had additional taxable income.

B. That the petitioners failed to sustain their burden of proof. Such failure resulted from the lack of testimony by persons who had personal knowledge of the relevant facts which could support a decrease in the "applications" noted in Findings of Fact "11" and "13" or which could provide an explanation for additional non-taxable "sources" of income.

It is noted that petitioners did not provide an adequate foundation or basis for the evidence which is detailed in Finding of Fact "16", supra. For example, little weight can be given to an unsigned typewritten promissory note without supporting testimony of either the borrower or lender.

C. That we note, however, that the Audit Division incorrectly determined the cash living expenses of petitioners Richard and Nancy Cargain by including an allocation for "Additional based on consistent drawings of both brothers." Therefore, the Audit Division is directed to redetermine the cash living expenses of such petitioners by decreasing their living expenses for 1977 and 1978 by \$4,392 and \$5,112, respectively, which will result in a decrease in the total application for each year at issue and a reduction in the "difference to be explained" for each year by the same amounts, \$4,392 and \$5,112, respectively.

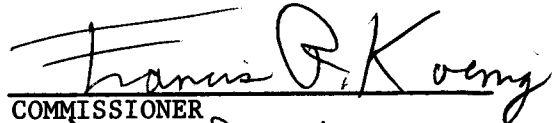
D. That the Audit Division is directed to modify (i) the Notices of Deficiency against petitioners Richard and Nancy Cargain and (ii) the Notices of Deficiency against petitioner Cargain Service Station, Inc. in accordance with Conclusion of Law "C", supra, but in all other respects, the petition of Cargain Service Station, Inc. and the petition of Richard and Nancy Cargain are denied. The petition of George Cargain is denied in full.

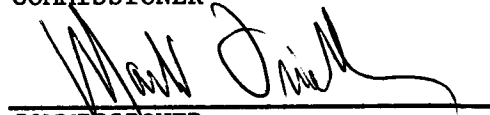
DATED: Albany, New York

STATE TAX COMMISSION

MAR 14 1985


PRESIDENT


COMMISSIONER


COMMISSIONER