

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Michael III & Carol Schiraldi :
for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Personal Income :
& Unincorporated Business Taxes under Articles 22 :
& 23 of the Tax Law for the Years 1975 & 1976. :
_____ :

AFFIDAVIT OF MAILING

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 21st day of March, 1984, he served the within notice of Decision by certified mail upon Michael III & Carol Schiraldi, the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Michael III & Carol Schiraldi
14 Oak Shore Drive
Bayville, NY 11709

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.

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

Sworn to before me this
21st day of March, 1984.

David Parchuck

James A. Schiraldi
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

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In the Matter of the Petition :
of :
Michael III & Carol Schiraldi :

AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Personal Income :
& Unincorporated Business Tax under Article 22 & :
23 of the Tax Law for the Years 1975 & 1976. :

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 21st day of March, 1984, he served the within notice of Decision by certified mail upon Vincent J. Cuti, the representative of the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Vincent J. Cuti
464 New York Ave.
Huntington, NY 11743

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.

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
21st day of March, 1984.

David Parchuck

James A. [Signature]
Authorized to administer oaths
pursuant to Tax Law section 174

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

March 21, 1984

Michael III & Carol Schiraldi
14 Oak Shore Drive
Bayville, NY 11709

Dear Mr. & Mrs. Schiraldi:

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 & 722 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
Vincent J. Cuti
464 New York Ave.
Huntington, NY 11743
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
of	:	
MICHAEL SCHIRALDI III AND CAROL SCHIRALDI	:	DECISION
for Redetermination of a Deficiency or for	:	
Refund of Personal Income and Unincorporated	:	
Business Taxes under Articles 22 and 23 of the	:	
Tax Law for the Years 1975 and 1976.	:	

Petitioners, Michael Schiraldi III and Carol Schiraldi, 14 Oak Shore Drive, Bayville, New York 11709, filed a petition for redetermination of a deficiency or for refund of personal income and unincorporated business taxes under Articles 22 and 23 of the Tax Law for the years 1975 and 1976 (File No. 32963).

A small claims 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 June 23, 1983 at 9:15 A.M. Petitioner Michael Schiraldi III appeared with Vincent J. Cuti, Esq. The Audit Division appeared by John P. Dugan, Esq. (Paul Lefebvre, Esq., of counsel).

ISSUES

- I. Whether adjustments made to petitioners' claimed telephone and automobile expenses were proper.
- II. Whether an adjustment made to purchases, for merchandise withdrawn for personal use, was proper.
- III. Whether petitioner is properly entitled to a depreciation deduction on a covenant not to compete.

FINDINGS OF FACT

1. Michael Schiraldi III (hereinafter petitioner) and Carol Schiraldi, timely filed a joint New York State Income Tax Resident Return for each of the years 1975 and 1976. In conjunction therewith, they filed a New York State Unincorporated Business Tax Return for each of said years whereon they reported their income and deductions attributable to their liquor store business, Birch Hill Liquors, 173 Birch Hill Road, Locust Valley, New York. Said business was operated as a sole proprietorship.

2. On May 30, 1980, as the result of a field audit, the Audit Division issued a Statement of Personal Income Tax Audit Changes wherein the following adjustments were made:

	<u>1975</u>	<u>1976</u>
"Telephone - not ordinary or necessary business expense	\$ 385.00	\$ 331.00
Car Expense - not ordinary or necessary business expense	727.00	2,153.00
Purchases - merchandise used for personal use	500.00	500.00
Depreciation (Covenant not to compete - there was no intention to compete at time of contract)	2,500.00	2,500.00
Rental Expense - gardening	231.00	130.00
20% Capital Gain Modification - net long term capital gains are taxed by New York State at 60% instead of 50%. Accordingly 20% of capital gains deduction must be added to income		<u>28.00</u>
Net Adjustment	<u>\$4,343.00</u>	<u>\$5,642.00"</u>

3. On May 30, 1980 the Audit Division also issued a Statement of Unincorporated Business Tax Audit Changes wherein the aforestated adjustments to telephone, car expenses, purchases and depreciation were made for unincorporated business tax purposes. Additionally, an adjustment was made to business contributions of \$717.00 for 1975 and \$532.00 for 1976. Said adjustment represented the unsubstantiated excess contributions claimed for unincorporated business tax purposes over

those claimed for personal income tax purposes. Accordingly, a Notice of Deficiency was issued against petitioners on March 20, 1981 asserting additional personal income tax of \$778.13, additional unincorporated business tax of \$578.22, plus penalty and interest of \$563.72, for a total due of \$1,920.07. Said penalty was asserted under section 685(c) of the Tax Law for failure to file a declaration of estimated personal income tax.

4. On January 4, 1979 and April 3, 1980 petitioners executed consent forms which extended the period for assessment to any time on or before April 15, 1981.

5. Petitioner conceded the adjustments to rental expense. The adjustments to contributions and the 20% capital gain modification were not challenged by petitioner.

6. Petitioners claimed 100% of their home and business telephone expenses for 1975 and 1976 as a business deduction. On audit, the Audit Division disallowed one third of such expenses as personal. At the hearing held herein, petitioner alleged that ninety to ninety-five percent of their telephone expenses were attributable to business purposes, however, no documentation was submitted to support such allegation.

7. Petitioners claimed 100% of their automobile expenses attributable to two cars as a business deduction during the years at issue. On audit, the Audit Division reduced their claimed 1976 automobile expense by \$793.00 since said amount represented a down payment on the purchase of a new automobile. Twenty-five percent of both the balance for 1976 and the deduction claimed for 1975 were disallowed as personal.

8. Petitioners alleged that they had two station wagons which they used for making deliveries and commuting to and from the store on a daily basis.

Each petitioner purportedly used one station wagon for the six mile daily round trip. Additionally, they owned a third automobile which they contended was used solely for personal purposes. The expenses attributable to this auto were not deducted on their return. Petitioner offered no documentation to establish the extent to which each station wagon was used for business purposes.

9. In computing the cost of goods sold for Birch Hill Liquors, petitioner used 100% of purchases for each year at issue. On audit, the Audit Division disallowed \$500.00 of purchases for each year as being withdrawn for personal use. Petitioner testified that the only time he withdrew wine from the business was for the purpose of tasting and evaluating so that he could properly serve his customers, since he sold a large quantity of expensive wines. He claimed that he never withdrew liquor from the business for personal consumption or for gifts since the samples he was given were used for these purposes.

10. Petitioner purchased the liquor store at 173 Birch Hill Road from his father, Michael Schiraldi, Jr., under the terms of a sales agreement entered into on July 9, 1970. Pursuant to such agreement, "The Seller will sell and the Buyer will buy the fixtures and equipment owned by the Seller at the above premises for the agreed price of \$50,000.00."

11. Pursuant to an undated rider, which petitioner testified was executed on the same date as the sales agreement, the \$50,000.00 purchase price "shall be allocated as follows:

1. Furniture and fixtures as detailed in the attached list (\$20,000) twenty thousand dollars.
2. For the good name of the business and the good reputation of the name Birch Hill Liquors (\$5,000) five thousand dollars.
3. In appreciation of the reputation of Michael Schiraldi, Jr. and the business his name can draw, the sum of (\$25,000) twenty five thousand dollars to not operate a liquor business within (10) miles of Locust Valley for a period of ten years."

12. Inventory was determined and paid for separately at the time of closing on September 1, 1970.

13. On his unincorporated business tax returns for the years at issue, petitioner claimed depreciation of \$2,500.00 each year on a "covenant not to compete".

14. On audit, the Audit Division disallowed the depreciation on the ground that it had not been established that the amount allocated to the covenant was for anything other than goodwill in the sale of the business.

15. Petitioner testified that his father is a "strict businessman," "difficult" and they "don't see eye to eye". He contended that he would not have purchased the business without the covenant not to compete.

16. Petitioner claimed that he had no knowledge of whether his father would have attempted to compete had he not secured the covenant. He claimed that his father's name and reputation were such that had he allowed his father to compete, his business would have suffered greatly.

17. Petitioner was unable to establish that had he not secured the covenant, his father would have been able to effectively compete under the State Liquor Authority location restrictions.

18. Petitioner testified that his father was fifty years old at the time of sale.

19. The business was not appraised by competent authority at the time of sale.

CONCLUSIONS OF LAW

A. That the adjustments to rental expense are sustained as conceded by petitioner.

B. That the adjustments to business contributions and the 20% capital gain modification are sustained since they were not challenged by petitioner.

C. That petitioner has failed to sustain his burden of proof, required pursuant to sections 689(e) and 722(a) of the Tax Law, to show that the adjustments made to telephone expenses, automobile expenses and purchases were improper or erroneous. Accordingly, said adjustments are sustained.

D. That where a covenant not to compete accompanies the transfer of goodwill in the sale of a going concern, and such covenant is essentially to insure the purchaser the beneficial enjoyment of the goodwill he has acquired, the covenant has been held by the Tax Court to be nonseverable and not subject to the allowance for depreciation. (Aaron Michaels, 12 T.C. 17,) Such result has been reached even when the contract placed a value on the covenant not to compete. (Toledo Blade Co., 11 T.C. 1079 Aff'd without opinion, (CA-6) 50-1 USTC ¶ 9234, 180 F. 2d 357.) On the other hand, where the taxpayer would not have been willing to purchase the business without the covenant and would not have paid the price it did unless the covenant was included, the court held that the price paid for the covenant not to compete could be segregated and depreciated. (Wilson Athletic Goods Mfg. Co., Inc., (CA-7) 55-1 USTC ¶ 9442, 222 F.2d 355.)

E. That petitioner has failed to sustain his burden of proof, required pursuant to sections 689(e) and 722(a) of the Tax Law, to show that he would not have been willing to purchase the business without the covenant and would not have paid the price he did unless the covenant was included. Further, he failed to show that his father had the intention or the ability to compete at the time of sale. Accordingly, the depreciation deductions claimed on the "covenant not to compete" are not allowable.

F. That the petition of Michael Schiraldi III and Carol Schiraldi is denied and the Notice of Deficiency dated March 20, 1981 is sustained together with such additional penalties and interest as may be lawfully owing.

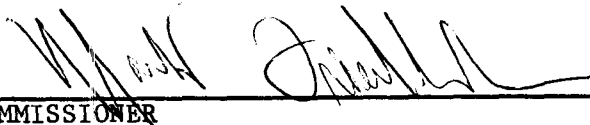
DATED: Albany, New York

STATE TAX COMMISSION

MAR 21 1984


PRESIDENT


COMMISSIONER


COMMISSIONER