

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Robert & Catherine Sandy :

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 1979 and 1980. :

In the Matter of the Petition :
of :
Green Shingle Inn :
(Catherine Sandy d/b/a Green Shingle Inn) :

for Revision of a Determination or for Refund of :
Sales & Use Taxes under Articles 28 and 29 of the :
Tax Law for the Period 12/1/78-11/30/81. :

AFFIDAVIT OF MAILING

State of New York :

ss.:

County of Albany :

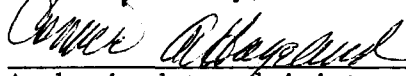
David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 29th day of May, 1985, he served the within notice of Decision by certified mail upon Robert & Catherine Sandy, the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Robert & Catherine Sandy
110 East Main St.
Elkland, PA 16920

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
29th day of May, 1985.


Authorized to administer oaths
pursuant to Tax Law section 174



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

May 29, 1985

Robert & Catherine Sandy
110 East Main St.
Elkland, PA 16920

Dear Mr. & Mrs. Sandy:

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
Donald W. Mustico
Mustico, Mustico & Ramich
304 Williams Street
Elmira, NY 14901
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Robert & Catherine Sandy :

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 :
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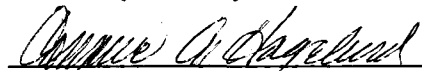
David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 29th day of May, 1985, he served the within notice of Decision by certified mail upon Green Shingle Inn, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Green Shingle Inn
110 East Main St.
Elkland, PA 16920

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
29th day of May, 1985.


Authorized to administer oaths
pursuant to Tax Law section 174



STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
Robert & Catherine Sandy :
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 1979 and 1980. :

AFFIDAVIT OF MAILING

In the Matter of the Petition :
of :
Green Shingle Inn :
(Catherine Sandy d/b/a Green Shingle Inn) :
for Revision of a Determination or for Refund of :
Sales & Use Taxes under Articles 28 and 29 of the :
Tax Law for the Period 12/1/78-11/30/81. :

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 29th day of May, 1985, he served the within notice of Decision by certified mail upon Donald W. Mustico, the representative of the petitioners in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Donald W. Mustico
Mustico, Mustico & Ramich
304 William Street
Elmira, NY 14901

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
29th day of May, 1985.

David Parchuck

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

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

May 29, 1985

Green Shingle Inn
110 East Main St.
Elkland, PA 16920

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) 1138 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
Donald W. Mustico
Mustico, Mustico & Ramich
304 William Street
Elmira, NY 14901
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
ROBERT SANDY AND CATHERINE SANDY :
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 1979 and 1980. :

DECISION

In the Matter of the Petition :
of :
GREEN SHINGLE INN :
(Catherine Sandy d/b/a Green Shingle Inn) :
for Revision of a Determination or for Refund :
of Sales and Use Taxes under Articles 28 and :
29 of the Tax Law for the Period December 1, :
1978 through November 30, 1981. :

Petitioners, Robert Sandy and Catherine Sandy, 110 East Main Street, Elkland, Pennsylvania, 16920, 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 1979 and 1980 (File Nos. 38700 and 38701).

Petitioner, Green Shingle Inn (Catherine Sandy d/b/a Green Shingle Inn), 110 East Main Street, Elkland, Pennsylvania, 16920, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 for the period December 1, 1978 through November 30, 1981 (File No. 38394).

A formal hearing was held before Dennis M. Galliher, Hearing Officer, at the offices of the State Tax Commission, 65 Court Street, Buffalo, New York, on August 21, 1984 at 1:15 P.M., with all briefs to be submitted by January 25, 1985. Petitioners appeared by Mustico, Mustico & Ramich, Esqs. (Donald W. Mustico, Esq., of counsel). The Audit Division appeared by John P. Dugan, Esq. (Deborah J. Dwyer, Esq., of counsel).

ISSUE

Whether the Audit Division's source and application of funds audit properly resulted in a finding of additional funds subject to personal income tax, unincorporated business tax and sales tax.

FINDINGS OF FACT

1. On June 30, 1982, the Audit Division issued a Notice of Deficiency to petitioner Catherine Sandy asserting additional personal income and unincorporated business taxes due for the years 1979 and 1980 in the aggregate amount of \$8,407.02, plus penalty and interest. On June 30, 1982, the Audit Division also issued a Notice of Deficiency to petitioner Robert Sandy asserting additional personal income tax due for the year 1979 in the amount of \$17.50, plus interest.

2. On March 19, 1982, the Audit Division issued to petitioner Green Shingle Inn (Catherine Sandy d/b/a Green Shingle Inn), a Notice of Determination and Demand For Payment of Sales and Use Taxes Due assessing additional sales tax due for the sales tax quarterly periods ended February 28, 1979 through November 30, 1981 in the aggregate amount of \$5,696.25, plus penalty and interest.

3. Petitioner Catherine Sandy has been involved in the tavern and restaurant business since 1939. From 1939 through 1948 she owned and operated, with her then-husband, William Jusick, a restaurant called Jusick's Restaurant located

in Tioga, Pennsylvania. Jusick's Restaurant was sold in 1948. In 1947, prior to the sale of Jusick's Restaurant, Mrs. Sandy purchased the Green Shingle Inn ("Green Shingle"), located on Route 15 in Lindley, New York. She has operated the Green Shingle as a sole proprietorship continuously since 1947. Mrs. Sandy was divorced from William Jusick in 1963 and married petitioner Robert Sandy in 1966. For a period of time, Mr. Sandy worked as an employee at the Green Shingle.

4. On or about November 6, 1981, the Audit Division commenced a field audit of Mr. and Mrs. Sandy and the Green Shingle, during the course of which several large deposits to savings and checking accounts were found. Since these deposits could not be traced back to any specific sources, such as withdrawals from the Green Shingle, etc., the auditor decided to perform a reconstruction of income by means of a source and application of funds audit analysis, the results of which may be summarized numerically as follows:

<u>Sources of Funds:</u>	<u>1979</u>	<u>1980</u>
Federal adjusted gross income (per 1040)	\$ 22,362.00	\$ 31,637.00
I.R.A. adjustment	1,375.00	1,351.00
Dividend Exclusion	200.00	200.00
Inheritance	5,828.00	-
Bank Mortgage Loan	20,000.00	-
Net Decrease in Checking Account	17,840.00	-
Net Decrease in Savings Accounts	-	3,699.00
<u>Withdrawals from Green Shingle</u>	<u>8,449.00</u>	<u>-</u>
<u>Total Funds Available:</u>	<u>\$ 76,054.00</u>	<u>\$ 36,887.00</u>

<u>Applications of Funds:</u>	<u>1979</u>	<u>1980</u>
Loan Repayments	\$ 20,145.00	\$ 19,081.00
Net Checking Account Increase	-	164.00
Net Savings Account Increase	12,113.00	-
Investments In Green Shingle	-	2,406.00

<u>Personal Living Expenses</u> ¹	<u>81,904.00</u>	<u>30,551.00</u>
Total Applications of Funds:	<u>\$114,162.00</u>	<u>\$ 52,202.00</u>
<u>Excess of Applications over Sources</u>	<u>\$ 38,108.00</u>	<u>\$ 15,315.00</u>

5. Since no apparent sources of income other than the Green Shingle existed, the Audit Division held the entire excess of applications over sources to be additional unreported income derived from operation of the Green Shingle and calculated the instant tax deficiencies based thereon.

6. Petitioners Robert and Catherine Sandy had timely filed New York State Income Tax Resident Returns (Forms IT-201) for 1979 and 1980, under filing status "3"; i.e. married filing separately on one return. It is noted that the deficiency asserted against Mr. Sandy reflects solely the disallowance of his claim for household credit [Tax Law §606(b)] upon the basis that the additional income found on audit increases the Sandys' household gross income to a level at which the household credit is unavailable.

7. The sales tax deficiency of \$5,696.25 was determined by dividing additional income found on audit, per year, by reported total sales, per year (per sales tax returns), to arrive at 44.123 percent for 1979 and 17.321 percent for 1981, respectively, as understated sales for each of such years. These respective percentages were applied as the margins of error to each of the sales tax returns filed for 1979 and 1980 to arrive at additional taxable sales per year.

1 Personal living expenses consisted of \$2,400.00 for food, \$1,500.00 for cash expenditures and \$1,000.00 in miscellaneous expenditures for each year, with the balance of expenses for each year consisting of expenditures made by Mrs. Sandy in remodeling her home.

For 1981, no actual audit work was performed. Rather, combined additional income found on audit for 1979 and 1980 (\$53,423.00) was divided by total reported sales (per sales tax returns) for such years (\$79,180.00) to arrive at 30.565 percent as average understated sales for such years. This percentage was then applied to the sales tax returns for 1981 to arrive at additional taxable sales for such year, upon the assertion that the understatement for 1979 and 1980 indicated the likelihood of understatement for 1981.

8. Petitioners do not contest the Audit Division's use of a source and application of funds analysis as an appropriate audit method. However, petitioners do challenge the sales tax projection into periods for which no actual audit work was done. Furthermore, petitioners allege the existence of other sources of funds available to Mrs. Sandy in 1979 which were not connected with or derived from sales by the Green Shingle during the subject years, as follows:

- a.) \$4,000.00: Sale of two acres of land;
- b.) \$11,000.00 (approximately): Sale of silver coins saved since 1964, receiving about \$3.00 for every \$1.00 in face value of coins sold;
- c.) \$1,200.00 (approximately): Sale of excess household furniture.

9. Mrs. Sandy also alleges the existence of a large cash hoard accumulated at home. This hoard was accumulated, in part, from savings during the years she had been in business. Furthermore, it is asserted that additional cash was available from certain specific transactions in prior years, including \$19,221.21 realized from the sale of stock in 1978, and \$1,850.54 from payment on a matured endowment insurance policy in 1978. Finally, petitioners assert a \$3,900.00 withdrawal from savings in 1979 was to pay prizes to winners of a baseball pool sponsored by the Green Shingle, that as set up the pool had

accumulated \$5,000.00 which was kept in cash at home by Mrs. Sandy, and that this pool constitutes an additional source of funds available in 1979.

10. At the commencement of the audit Mrs. Sandy was asked, in the presence of her then-accountant, whether she maintained a sum or hoard of cash at home. She indicated that such sum was never more than \$6,000.00.

11. Mrs. Sandy did not maintain records of the amounts flowing in and out of the alleged cash hoard over the years. She testified that she had been saving to buy a "dream house" and that she had never owned a house but had lived upstairs from her businesses all her life. The cash hoard, assertedly totalling between \$30,000.00 and \$40,000.00 prior to the purchase of a house in 1978, was kept in a safe in Mrs. Sandy's bedroom because Mrs. Sandy didn't want her second husband, petitioner Robert Sandy, to know about its existence.

12. The described cash hoard, as well as business cash receipts from the Green Shingle were kept in the same safe, and money therefrom was put into and taken out of the business according to cash needs. Mrs. Sandy testified that "[I] never kept track of what I took out exactly or what exactly was put in". With reference to the initial audit questions regarding a cash hoard she indicated that she apparently misunderstood and believed the question pertained only to business cash, and further that by the time of the audit (1981), much of her cash hoard had been used up on the house.

13. Marilyn Whitney, who worked at Green Shingle between 1969 and 1974 testified that Mrs. Sandy had told her she was saving for a dream house and, further, that she had seen silver coins and money inside Mrs. Sandy's safe. Mrs. Whitney did not know nor could she guess at the amount of money in the safe, stating only that it was in stacks and appeared to be a substantial amount. She had no knowledge of the alleged sale of silver in 1979.

14. No records, bills of sale or other documents were presented pertaining to the silver coins or furniture sold in 1979 (see Finding of Fact "8-b" and "8-c"), and the noted receipts therefrom are estimates as to the approximate amounts received on such sales.

15. Two checks totalling \$4,000.00 were presented with respect to the sale of two acres of land (see Finding of Fact "8-a"). The two acres were a part of a fifty acre tract of land with a burned-out house purchased by petitioners in or about 1975 for \$35,000.00. The \$4,000.00 payment checks consist of a \$400.00 check dated September 11, 1978 and a \$3,600.00 check dated March 24, 1979.

16. Petitioners assert that savings over a period of years, the stock sales in 1978, and the insurance policy payment indicate sources by which an available cash hoard was created. The total amount of such cash hoard was not precisely specified, but petitioners maintain that this hoard, together with the alleged furniture, coin and land sales in 1979 closely approximate the combined excess funds for both years as determined upon audit. Petitioners also note that since Schedule C expenses for Green Shingle for the years 1979 and 1980 did not vary significantly it is unreasonable to believe that Green Shingle sales varied by the additional amounts of income as found on audit for each of the years. Finally, petitioners assert that if the additional amounts determined on audit are held to be business receipts, they should nevertheless be reduced by the amount of sales tax collections inherent therein.

CONCLUSIONS OF LAW

A. That petitioners' assertions that the additional funds for 1979 and 1980 were cash items accumulated from activities during prior years and from sales of land, silver coins and excess furniture in 1979 are in large measure

unsubstantiated. Monies, both business and personal, were apparently freely commingled. No records were kept of amounts maintained at home and put into and pulled out of the business, nor could petitioners describe a definite amount of cash involved. The manner in which Mrs. Sandy chose to handle her finances left no accurate means of verifying amounts involved and petitioners must bear the consequences flowing therefrom.

B. That during 1979, \$3,600.00 was received on the sale of two acres of land as described, which amount was not included as a source of available funds in 1979. Although Mrs. Sandy testified to the existence of additional sources of funds, no definite dollar amounts of such funds were proven. Transactions occurring in prior years do not absolutely result in funds therefrom being available in later years, inasmuch as such funds may have been spent, re-invested or otherwise disposed of in such prior years. Accordingly, the only additional source of funds proven and allowable in reduction of audited additional taxable income for 1979 was the land sale receipt of \$3,600.00. For 1980, there has been no proof of any additional funds available in excess of those documented on audit, and thus no reduction of audited additional funds subject to tax is warranted.

C. That the portion of the sales tax assessment pertaining to 1981 is to be cancelled. A mere suspicion that there was underreporting for 1981, based on underreporting in 1979 and 1980, without any audit work whatsoever in support thereof is an insufficient basis for the assessment for 1981. However, with respect to 1979 (except as noted in Conclusion of Law "B") and 1980, there has been no proof that the excess funds found on audit were from any source other than sales by the Green Shingle and thus the imposition of personal income tax, unincorporated business tax and sales tax on such excess funds was

proper². Furthermore, there has been no proof of any sales tax remitted during 1979 or 1980 in excess of amounts reported per sales tax returns, and thus petitioners' assertion that additional income attributed to unreported sales by the Green Shingle necessarily included sales tax collected on such sales is unsupported and unpersuasive.


D. That notwithstanding the reduction for 1979 as specified in Conclusion of Law "B", Robert and Catherine Sandy's household gross income after audit is such that petitioners do not qualify for a household credit [Tax Law section 606(b)].

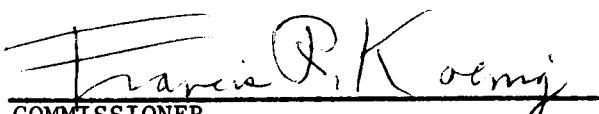
E. That the Notice of Deficiency issued to petitioner Catherine Sandy is to be recomputed in accordance with Conclusion of Law "B" and as recomputed is sustained. The Notice of Deficiency issued to petitioner Robert Sandy is, in accordance with Conclusion of Law "D", sustained. The Notice of Determination issued to Green Shingle Inn (Catherine Sandy d/b/a Green Shingle Inn) is to be recomputed in accordance with Conclusions of Law "B" and "C", and as recomputed is sustained.


DATED: Albany, New York

STATE TAX COMMISSION

MAY 29 1985


PRESIDENT


COMMISSIONER


COMMISSIONER

2 For purposes of recomputation in accordance herewith, basis in the two acres of property sold is to be determined in accordance with Finding of Fact "15".