STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
JOHN AND JILL MISKANIC	:	DETERMINATION DTA NO. 826550
for Redetermination of a Deficiency or for Refund of Personal Income Tax under Article 22 of the Tax Law for the Years 2010 and 2012.	:	

Petitioners, John and Jill Miskanic, 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 2010 and 2012.

On November 9, 2015 and November 18, 2015, respectively, petitioners, appearing by Robert Rettig, CPA, and the Division of Taxation, appearing by Amanda Hiller, Esq. (Linda Jordan-Harmonick, Esq., of counsel), waived a hearing and submitted the matter for determination based on documents and briefs to be submitted by March 21, 2016, which date began the six-month period for issuance of this determination. After due consideration of the documents and arguments submitted, Daniel J. Ranalli, Supervising Administrative Law Judge, renders the following determination.[1]

ISSUE

Whether the Division of Taxation properly determined additional personal income tax due from petitioners for the years 2010 and 2012.

[1]Upon the retirement from state service of the original administrative law judge, the case was transferred to the supervising administrative law judge.

FINDINGS OF FACT

1. John and Jill Miskanic (petitioners) filed New York State resident income tax returns for the years 2010 and 2012 (years in issue) as married filing jointly. For the year 2010, they requested and received a refund of $5,461.00, and for 2012 they requested and received a refund of $7,256.00. The latter included $1,571.00 attributable to an earned income credit. The Division of Taxation (Division) selected both of these returns for review.

2. After reviewing the 2010 return, the Division determined that the claimed business and rental losses could not be verified and disallowed them. To inform petitioners of these determinations, the Division issued a Statement of Proposed Audit Change, dated March 22, 2013, in which the business and rental losses were removed from the calculation of tax due, and the result was additional tax due of $2,020.00 plus penalty and interest.

After reviewing the 2012 return, the Division determined that, once again, the business and rental losses could not be verified and disallowed them. A Statement of Proposed Audit Change was issued to petitioners for the year 2012, dated July 18, 2013, asserting additional tax due of $4,257.00 plus penalty and interest.

Petitioners did not respond to the statements of proposed audit change, and the Division issued two notices of deficiency for the additional tax determined to be due for the years in issue. The first Notice of Deficiency, L-039165705-4, dated August 28, 2013, asserted additional income tax due for the year 2010 in the sum of $2,020.00 plus penalty and interest. The second notice, L-039682180-5, dated September 4, 2013, asserted additional tax due of $4,257.00 plus penalty and interest for the year 2012.

3. Petitioners contested the notices of deficiency by filing for a Bureau of Conciliation and Mediation Services (BCMS) Conference, which sustained the notices in an Order, dated July 18, 2014. This proceeding ensued.

4. At no time during the audit or BCMS proceedings did petitioners offer any documentary or other proof to support the business and rental losses claimed on their returns for the years in issue.

5. On July 1, 2010, petitioners incorporated a New Jersey S corporation, "Jack in the Box Entertainment, Inc." Petitioners were each listed as 50 percent shareholders of the corporation.

6. As part of the audit, the Division reviewed tax years 2010 through 2014, to determine if the claimed business activities were engaged in for profit. A summary of the Division's review of the returns filed by petitioners and information received from the Internal Revenue Service (IRS) is demonstrated by the following charts:

Year	Income before Losses	Schedule C Gross Income	Schedule C Expenses	Net Schedule C Claimed Loss
2010	$83,758.00	$1,505.00	($21,105.00)	($19,600.00)
2011	$87,569.00	N/A	N/A	N/A
2012	$90,211.00	$2,500.00	($71,034.00)	($68,534.00)
2013	$94,570.00	$2,500.00	($78,036.00)	($75,536.00)
2014	$105,852.00	$2,650.00	($91,391.00)	($88,741.00)

Year	S Corp Claimed Loss	Reported Rental Gross Income	Net Rental Claimed Loss	Reported New York AGI	Reported Taxable Income
2010	($31,588.00)	$31,200.00	($2,660.00)	$31,647.00	$0.00
2011	($45,128.00)	$31,200.00	($12,473.00)	$31,847.00	$0.00
2012	($35,489.00)	$31,200.00	($12,186.00)	$24,820.00	$0.00
2013	($2,500.00)	$31,200.00	($7,859.00)	$8,455.00	$0.00
2014	($5,430.00)	$31,200.00	($10,292.00)	$1,143.00	$0.00

7. Rental losses for both 2010 and 2012 were disallowed because petitioners provided no supporting documentation of any rental activities or actual expenses incurred. With respect to the business losses claimed on the schedules C (federal form 1040) and the losses set forth on the schedules E (federal form 1040) from the S corporation, the Division discovered numerous unexplained discrepancies.

The schedules C for 2010 and 2012 listed John Miskanic as the sole proprietor of a business. For 2010, the schedule C listed the business activity as entertainment, the business name as "Jack in the Box" and the business address as 20 Elizabeth Avenue, East Brunswick, New Jersey. The 2012 schedule C listed the business activity as "entertainment management" but listed no business name or address.

8. For 2010 and 2012, petitioners claimed business losses from the New Jersey S corporation, Jack in the Box Entertainment, Inc., which also listed an address of 20 Elizabeth Avenue, East Brunswick, New Jersey.

9. Because the schedule C business and the S corporation shared business activities, a business name and address, and John Miskanic played a significant role in each entity, the

Division could not distinguish between the two. The Division investigated the businesses but found no independent evidence of them on the Internet.

10. A review of petitioners' tax filings for the period 2010 through 2014, as set forth on the charts above, indicated that the S corporation reported a loss for all five years and the schedules C reflected a loss for all years except 2011, when petitioners did not file that schedule. Petitioners submitted no evidence that the schedule C business or the S corporation were being operated for profit. The schedule C business's gross income was modest, ranging from $1,505.00 to $2,650.00 during the years 2010 through 2014 ($1,505.00 in 2010 and $2,500.00 in 2012), yet even these amounts were unsubstantiated. On the other hand, the reported losses, which increased each year, were approximately 13 times earnings in 2010 and 27.5 times earnings in 2012.

11. Petitioners did not submit their S corporation tax returns into evidence, but the transcript of the filing for 2012 was provided to the Division by the IRS and listed gross receipts of $1,500.00.

12. To substantiate their deductions, petitioners submitted two years of bank statements from TD Bank for the years 2010 and 2012. With the submission, a letter from petitioners' representative explained that the deductions had been taken on their federal S corporation returns and on schedule C of their individual tax returns. Petitioners' representative highlighted various items on the bank records, for a convenience checking account in petitioners' names, which purportedly indicated ATM/debit withdrawals for business purposes, automobile, gasoline and travel expenses and credit card payments, the latter purportedly for wardrobe, costumes and public relations.

13. Based on these bank statements, petitioners concluded that they had properly substantiated the expenses listed on the schedule Cs and the S corporation returns for both years in issue. The following chart summarizes petitioners' figures:

Year	Amount per Return	Substantiation	Difference
2010 - Expenses S Corporation	$24,300.00	$24,300.00	$0.00
2010 - Expenses Schedule C	$21,107.00	$22,770.00	$1,663.00
2012 - Expenses S Corporation	$36,989.00	$35,549.00	($1,440.00)
2012 - Expenses Schedule C	$71,000.00	$68,270.00	($2,730.00)

14. The Division's analysis of petitioners' bank records did not change its position with regard to the validity of the expenses claimed. For all the entries on the bank statements that represented ATM withdrawals, the Division noted that there was no way to discern how the cash withdrawals were used, let alone that they were used for any valid business purpose.

The entries that were highlighted as wardrobe, costumes and public relations, were not considered valid business expenses by the Division since the entries on the bank statements merely indicated payments to credit card companies.

For those expenses labeled "[a]uto, gas and travel," the Division agreed that such expenditures may be legitimate business expenses, but there must also be a showing that the expenses were made in connection with the production of income or that are ordinary and necessary to the business activity. Since no such showing was made by petitioners, these expenses were denied. Charges for telecommunications were also denied on the same basis.

15. The Division was never provided with any documentation to prove that petitioners were engaged in an activity for profit or the specific nature of the business activity.

16. Petitioners provided no evidence of the business activity they claim to have entered into for profit, with the exception of a letter written by their representative as part of his written argument herein. In that letter, it was stated that petitioners created the S corporation to manage the entertainment career of their daughter and that all the expenses were incurred in the management of her career. Petitioners submitted a contestant agreement, personal release and arbitration agreement, dated June 20, 2015, to participate in the "American Idol" television talent show. Presumably, this was to demonstrate that petitioners' daughter was pursuing an entertainment career. No other evidence or explanation of the business activity was introduced into the record.

SUMMARY OF THE PARTIES' POSITIONS

17. Petitioners focus on a list of nine factors they believe are relevant in determining whether their business activity was conducted with the intent to earn a profit, relying chiefly on ***Crile v. Commissioner*** (TC Memo 2014-202 [where the United States Tax Court held that an artist and tenured art professor of studio art was engaged in an activity for profit and engaged in a trade or business for profit, relying on the nine factors listed in Treas Reg § 1.183-2(b) and noting the scope of her business activity and the testimony of four experts]).

These nine factors are rooted in Treas Reg § 1.183-2(b), which states that the nonexclusive list of factors that can be used to ascertain if a taxpayer conducted an activity with the intent to earn a profit are as follows: the manner in which the taxpayer conducts the activity; the expertise of the taxpayer or his or her advisors; the time and effort spent by the taxpayer in carrying on the activity; the expectation that assets used in the activity may appreciate in value; the success of the

taxpayer in carrying on other similar or dissimilar activities; the taxpayer's history of income or losses with respect to the activity; the amount of occasional profits, if any; the financial status of the taxpayer; and elements of personal pleasure or recreation.

Petitioners maintain that all nine factors strongly support the conclusion that they were engaged in an activity with the honest expectation of earning a profit, and therefore have met their burden of proof.

18. The Division contends that petitioners have not met their burden of proof because they have not established the business losses they claimed.

The Division argues that there is a presumption created by IRC § 183(d) that an activity will be seen as engaged in for profit if the gross income for three or more years in the period of five consecutive years exceeds the deductions attributable to such activity. Since this was not the case here, i.e., the activity did not generate gross income in excess of deductions for any of the five years analyzed by the Division, there is no presumption of profitability, and petitioners have not submitted any other proof to establish that the activity was engaged in for profit.

CONCLUSIONS OF LAW

A. A properly issued notice of deficiency is presumed to be correct, and the taxpayer has the burden of demonstrating the incorrectness of such an assessment (***Matter of Leogrande v. Tax Appeals Tribunal***, 187 AD2d 768, 589 NYS2d 383 [1992], ***lv denied*** 81 NY2d 704 [1993]). Tax Law § 689(e) provides that in any matter brought before the Division of Tax Appeals under Article 22 of the Tax Law, the burden of proof is upon the petitioner. Accordingly, it is necessary to ascertain whether petitioners have sustained their burden of proof in showing that they owe no additional personal income tax for the years 2010 and 2012.

B. Petitioners were required to keep records to establish the amount of gross income and credits reported on their 2010 and 2012 New York tax returns (20 NYCRR 158.1[a]) and to produce them when requested (20 NYCRR 158.7). When petitioners were asked to substantiate the business income and expenses taken on their schedule Cs and the pass through losses emanating from their S corporation for 2010 and 2012, they initially produced no documentation at all, and then only submitted bank records for a personal bank account. Their submission is woefully deficient and fails to substantiate any of the losses claimed on either the schedule C or S corporation returns.

Petitioners have not submitted any credible evidence of the business activity engaged in for profit. The only information provided to this forum came in the form of a letter submitted in lieu of a brief in which, in less than one paragraph, the business activity was described by petitioners' representative as management of the entertainment career of their daughter. The only evidence of their daughter's career was a contestant agreement, personal release and arbitration agreement, dated June 20, 2015, to participate in the "American Idol" television talent show.

The only substantiating documentation submitted was two years of bank statements, with various charges to the account highlighted by petitioners' representative with self-serving explanations that attributed the charges to business expenses incurred by petitioners, which amounted to pure speculation. Not once did the representative explain his personal knowledge of the petitioners' business activity or how he was able to identify the charges to the bank account as business expenses with such specificity. Although given the opportunity to submit sworn affidavits, petitioners chose to remain silent and provided no explanation of their business activities, which provided a significant shelter for their income. This is quite remarkable, considering the fact that they declared income before losses in 2010 of $83,758.00 and, after

accounting for their schedule C and S corporation losses, had no taxable income whatsoever. Similarly, for 2012, petitioners declared income before losses of $90,211.00, but had no taxable income after accounting for the schedule C and S corporation losses.

Petitioners' documentation of their claimed business expenses, the bank records, failed to show that said expenses were in fact business related, rather than personal (***Matter of Temple***, Tax Appeals Tribunal, July 8, 2004). Therefore, it is not necessary to seriously consider the analysis in the ***Crile*** case cited by petitioners, which discussed the application of the nine-point test used to ascertain if a taxpayer conducted an activity with the intent to earn a profit (Treas Reg § 1.183-2[b]). Petitioners were required to show that their circumstances presented a factual landscape that would lend itself to such an analysis. Here, petitioners have not provided the Division or this forum with any facts upon which a determination could be granted in their favor.

Although the Division has tried to structure arguments in its brief that assume facts not in evidence, this forum will not attempt to do the same. Petitioners simply have not offered any evidence to establish even the most basic facts necessary to analyze whether a legitimate business activity was carried on and whether the expenses incurred with respect to that activity were valid and proper (***see Matter of Crile***).

When the parties choose to waive their right to a hearing and proceed on the submission of documents, which may include sworn affidavits, and written legal argument, there is always the possibility that critical facts may not be introduced or adequately substantiated. Here, there was a complete failure to present a factual framework upon which a determination could be made on the issues of whether a valid business activity existed or if the losses claimed were proper.

Given the numerous opportunities afforded petitioners to produce evidence in support of their losses and expenses, and their failure to do so, the Division's disallowance of said deductions must be upheld (***Matter of Sperl***, Tax Appeals Tribunal, May 8, 2014).

C. The petition of John and Jill Miskanic is denied and the notices of deficiency, dated August 28, 2013 and September 4, 2013, are sustained.

DATED: Albany, New York
September 15, 2016

/s/ Daniel J. Ranalli
ADMINISTRATIVE LAW JUDGE