

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition	:	
of	:	
<b>EMILIO BRANCHINELLI</b>	:	DETERMINATION
	:	DTA NO. 828861
for Redetermination of a Deficiency or for Refund of New York State Personal Income Tax under Article 22 of the Tax Law for the Years 2010, 2011 and 2012.	:	

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Petitioner, Emilio Branchinelli, filed a petition for redetermination of a deficiency or for refund of New York State personal income tax under article 22 of the Tax Law for the years 2010, 2011 and 2012.

A videoconferencing hearing via CISCO Webex was held before James Connolly, Administrative Law Judge, on February 25, 2021 with all briefs to be submitted by July 16, 2021, which date began the six-month period for the issuance of this determination. Petitioner appeared by Barton LLP (Alvan L. Bobrow, Esq., of counsel). The Division of Taxation appeared by Amanda Hiller, Esq. (Michele W. Milavec, Esq., of counsel). Pursuant to 20 NYCRR 3000.15 (f), the case was reassigned to Kevin R. Law, Administrative Law Judge, who renders the following determination.

***ISSUES***

I. Whether the Division of Taxation properly asserted additional income tax due by using the results of a previous sales tax audit.

II. Whether penalties asserted should be abated.

***FINDINGS OF FACT***

1. During the tax years 2010 through 2012, petitioner, Emilio Branchinelli, was a shareholder in a number of S corporations, including Absolutely Italian Food Corporation (Absolutely Italian) and Primamore Italian Food Corporation (Primamore), and reported the income, gains, and losses from his ownership interests on his New York State resident personal income tax returns filed for those years.

2. Specifically, petitioner was a 34% shareholder in Absolutely Italian and a 50% shareholder in Primamore. Both entities were federal and New York State S corporations and each operated as an Italian restaurant in New York.

3. As is relevant herein, petitioner reported on his New York State resident income tax returns schedule E income of \$294,926.00 in 2010, claimed a schedule E loss of \$844,229.00 in 2011, and reported schedule E income of \$394,220.00 in 2012. Petitioner also claimed a net operating loss (NOL) from a prior year in the amount of \$266,557.00 on his 2012 return.

4. The Division conducted sales tax audits of both Primamore and Absolutely Italian for the period December 1, 2009 through August 31, 2012.

5. The sales tax audit of Primamore found additional taxable sales of \$2,458,065.28 and, consequently, the Division asserted additional sales tax due in the amount of \$212,008.13, and tax on capital of \$4,279.79, plus penalties and interest. The sales tax asserted due was determined based upon an observation of the restaurant and use of a cash to credit ratio to estimate sales over the audit period. The record does not disclose why a detailed audit of Primamore was not conducted.

6. The sales tax audit of Absolutely Italian found additional taxable sales of \$1,494,502.96 and, consequently, additional tax on sales asserted due in the amount of

\$128,900.86, plus tax on capital of \$1,625.95. An estimated audit methodology was utilized because a detailed audit could not be performed as sales records were deemed inadequate. The sales tax asserted due was determined based upon an observation of the restaurant and use of a cash to credit ratio to estimate sales over the audit period. Specifically, no source records were provided for the entire audit period.

7. On October 27, 2015, the Division issued notice of determination L-043878117 to Absolutely Italian asserting sales tax of \$130,530.81 plus penalties and interest. On that same date, the Division issued notice of determination L-043878121 to Primamore asserting sales tax of \$216,287.92 plus penalties and interest

8. On May 6, 2016, following a conciliation conference in the Division's Bureau of Conciliation and Mediation Services (BCMS), Absolutely Italian executed a consent settling notice of determination L-043878117, agreeing to tax in the amount of \$51,770.18 plus interest. The penalties were abated. The agreed tax was based upon additional taxable sales of \$581,335.95 for the audit period yielding additional tax of \$50,140.23 plus tax on capital of \$1,629.95.

9. On May 6, 2016, Primamore executed a consent at BCMS for notice of determination L-043878121 agreeing to tax in the amount of \$121,539.55 plus interest. Penalties were abated. The agreed tax was based upon additional taxable sales of \$1,359,533.39 for the audit period, yielding additional tax of \$117,259.76 plus tax on capital of \$4,279.79.

10. The Division's sales tax auditors referred the sales tax audit results for both Absolutely Italian and Primamore to the Division's income/franchise tax auditors for income tax audits. Based upon the sales tax audits, the Division's income/franchise auditors determined that Absolutely Italian and Primamore had underreported their gross sales in tax years 2010, 2011

and 2012. After an allowance for cost of goods sold, the Division determined additional ordinary income to petitioner in the amount of \$118,861.00 in 2010, \$315,426.00 in 2011, and \$174,834.00 in 2012.<sup>1</sup>

11. The Division also requested that petitioner substantiate the \$844,229.00 schedule E loss claimed in tax year 2011 and the \$266,557.00 NOL he claimed in tax year 2012.

12. Petitioner asserted that the schedule E loss in 2011, and the NOL in 2012, was a result of his ownership of Tutto Fresca Italian Food, LLC (Tutto Fresca), a limited liability company taxed as a partnership. Petitioner owned a 57.14% interest in Tutto Fresca during tax year 2011. Petitioner did not provide any substantiation of his basis in Tutto Fresca upon request by the Division.

13. Consequently, the Division adjusted petitioner's personal income tax returns for the tax years 2010, 2011, and 2012 to reflect the increased ordinary income from Absolutely Italian and Primamore, disallowed the claimed Schedule E loss for tax year 2011, and disallowed the claimed NOL in tax year 2012, as follows:

Year	2010	2011	2012
Additional Income from Primamore	\$113,232.00	\$265,282.00	\$165,006.00
Additional Income from Absolutely Italian	\$5,629.00	\$50,144.00	\$9,828.00
Disallowed Schedule E loss		\$844,229.00	
Disallowed NOL			\$266,557.00

14. The Division issued a notice of deficiency L-045676023, dated November 14, 2016, asserting \$150,261.00 in tax plus interest, and negligence penalties pursuant to Tax Law § 685 (b) (1) and (2), for the tax years 2010, 2011, and 2012.

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<sup>1</sup> Because petitioner was a shareholder in both Absolutely Italian and Primamore, the increased ordinary income of both S corporations flowed through to petitioner's personal income tax returns in the respective tax years.

15. Following a conciliation conference in BCMS, a conciliation order sustaining the notice of deficiency was issued.

16. Subsequently, petitioner submitted additional documentation to the Division substantiating \$240,000.00 of capital contributions to Tutto Fresca. The Division concedes that the \$240,000.00 in capital contributions to Tutto Fresca results in an adjustment to the notice of deficiency to allow \$240,000.00 of the \$844,229.00 schedule E loss originally disallowed for the 2011 tax year. Consequently, the tax asserted, as revised, is \$128,733.00 plus interest and negligence penalties.

17. The Division presented the testimony of its income tax auditor who was responsible for issuance of the notice of deficiency. The auditor explained the factual basis thereof. Upon cross-examination, the auditor testified that sales tax audits are referred for income tax audits when the results of sales tax audits are “substantial.” He was unable, however, to articulate or quantify when such results are deemed “substantial.” No further evidence was presented by either party on this issue.

18. Pursuant to section 307 (1) of the State Administrative Procedure Act and 20 NYCRR 3000.15 (d) (6), the Division submitted 20 proposed findings of fact. Proposed findings of fact 1 through 4 and 7 through 20 of the proposed findings of fact are supported by the record, and have been consolidated, condensed, combined, renumbered and substantially incorporated herein (*see* State Administrative Procedure Act § 307 [1]). Proposed findings of fact 5 and 6 have been accepted in part and rejected in part as conclusory, irrelevant and/or not supported by the record; to the extent accepted they have been consolidated, condensed, combined, renumbered and substantially incorporated herein (*id.*).

### **CONCLUSIONS OF LAW**

A. A properly issued notice of deficiency carries with it a presumption of correctness (*Matter of Tavolacci v State Tax Commn.*, 77 AD2d 759 [3d Dept 1980]; *Matter of Denn*, Tax Appeals Tribunal, October 25, 1990). The burden of proving that the notice is incorrect or erroneous lies with petitioner (Tax Law § 689 [e]). Where there is some factual basis for deciding that tax returns, as filed, do not accurately reflect the true income received by a taxpayer, the Division may determine proper income by using an indirect audit method (*see* Tax Law § 681 [a]; *Holland v United States*, 348 US 121, 131-132 [1954]; *Hennekens v State Tax Commn.*, 114 AD2d 599 [3d Dept 1985]). In this case, the Division utilized the results of the sales tax audits of Absolutely Italian and Primamore to assert additional income to petitioner in accordance with his ownership interest in said entities. The determination of additional sales in those audits provided a factual basis for the Division to decide that the income reported by petitioner on his personal income tax returns was not accurate (*see Matter of Rosemellia*, Tax Appeals Tribunal, March 12, 1992; *Matter of Bonanno*, Tax Appeals Tribunal, December 13, 1990; *Matter of Bruno*, Tax Appeals Tribunal, May 13, 1993; *Matter of Bok Hui Nam*, Tax Appeals Tribunal, September 24, 2009). In this case, since petitioner offered no evidence in an attempt to meet his burden of proving that the notice of deficiency is incorrect, he has surrendered to its presumption of correctness (*Matter of Leogrande*, 187 AD2d 768 [3d Dept 1992], *lv denied* 81 NY2d 704 [1993]; *Matter of Tavolacci*).

B. Petitioner does not dispute the use of a one-day observation to estimate sales tax of Absolutely Italian and Primamore, but contends that further extending the results of that methodology to attribute additional income to him is unreasonable. This argument is the same argument advanced by the petitioner and rejected by the Tax Appeals Tribunal in *Matter of Bok*

**Hui Nam.** It is also rejected herein as petitioner has advanced no compelling reason why a different conclusion is warranted.

C. Petitioner also alleges that referral of only those sales tax audits involving substantial underreporting of sales results is an equal protection violation because he is being treated differently than a restaurant whose audit results were not substantial. Petitioner's claim is rejected as he has not shown a purposeful, invidious, and intentionally unfair discrimination in the enforcement of the income tax laws (*see Di Maggio v Brown*, 19 NY2d 283 [1967]; *People v Friedman*, 302 NY 75 [1950], *appeal dismissed* 341 US 907 [1951]; *Matter of Doe v Coughlin*, 71 NY2d 48 [1987]). Equal protection does not require identical treatment. It only requires that classification rest on some real and not feigned differences, that the distinction have some relevance to the purpose for which the classification is made, and that the different treatments be not so disparate, relative to the difference in classification, as to be wholly arbitrary (*see Walters v St. Louis*, 347 US 231, 237 [1954]). The fact that the results of a sales tax audit are only referred for an income tax audit when the underreporting is "substantial" is certainly reasonable based upon limited government resources. Petitioner has not shown the differing treatment to be wholly arbitrary.

D. Petitioner, without citation to any authority, further asserts that the deficiency should be cancelled as the referral of the results of a sales tax audit for an income tax audit, where substantial underreporting of sales is determined, constitutes de facto rule making under the State Administrative Procedure Act (SAPA). Petitioner's unsupported assertion is rejected. For purposes of SAPA, "[a] rule announces a fixed general principle that is applied by an administrative agency without regard to other facts and circumstances relevant to the regulatory scheme of the statute the agency administers" (*Matter of Taylor v New York State Dept of*

*Correctional Services*, 248 AD2d 799, 800 [3d Dept 1998], citing *Matter of New York City Tr. Auth. v New York State Dept. of Labor*, 88 NY2d 225, 229 [1996]). Here, there is no evidence in the record that demonstrates that referral is mandated in all circumstances, nor does it appear, based upon the limited record herein, that the policy of referring sales tax audit results for income tax audits is based upon a quasi-legislative edict by the Division (*see Alca Industries, Inc. v Delaney*, 92 NY2d 775, 778 [1999]). Additionally, the referral of sales tax audit results for income tax audits appears to be the Division's internal audit policy not directly affecting the general public, and therefore not within the ambit of SAPA (*see* SAPA § 102 [2] [b] [i]; *Matter of Taylor*).

E. Finally, the Division imposed negligence penalties pursuant to Tax Law § 685 (b) (1) and (2), which provides that if any part of a deficiency is due to negligence or intentional disregard of the Tax Law, a penalty equal to 5% of the deficiency and 50% of the interest payable shall be imposed. Petitioner offered no evidence at the hearing on this issue but asserts that the cooperation advanced at audit as documented in the audit file demonstrates that the deficiency was not due to negligence nor intentional disregard of the Tax Law. This argument is without merit and is irrelevant to the inquiry as to whether petitioner's filings were negligent at the time the same were made. Extending cooperation to the auditor in conducting an audit is no more than what should be the expected, and accepted, norm. While it is acknowledged that penalties on the sales tax notices of determination issued to Absolutely Italian and Primamore were abated in accordance with consents settling the matters at BCMS, a portion of the income tax deficiency at issue herein stems from petitioner's failure to substantiate \$604,229.00 of the schedule E loss claimed by petitioner on his 2011 personal income tax return. It simply cannot be stressed enough that petitioner has simply not met his burden of establishing that the



deficiency was not based on negligence or intentional disregard of the Tax Law based upon his failure to introduce any documentary evidence or testimony at hearing. The penalties are therefore sustained.

F. The petition of Emilio Branchinelli is denied, and the November 14, 2016 notice of deficiency, as modified (*see* finding of fact 16), is sustained.

DATED: Albany, New York  
January 13, 2022

/s/ Kevin R. Law  
ADMINISTRATIVE LAW JUDGE