

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

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In the Matter of the Petition :

of :

**CHARALAMBOS AND PARASKEVI BALLIS** :

DECISION  
DTA NO. 814182

for Redetermination of a Deficiency or for Refund of New York State and New York City Personal Income Taxes under Article 22 of the Tax Law and the New York City Administrative Code for the Years 1983 and 1984. :

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The Division of Taxation filed an exception to the amended determination of the Administrative Law Judge issued on February 20, 1997 with respect to the petition of Charalambos and Paraskevi Ballis, 15-74 216<sup>th</sup> Street, Bayside, New York 11360. Petitioners appeared *pro se*. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Paul Lefebvre, Esq., of counsel).

The Division of Taxation filed a brief in support of its exception. Petitioners did not file a brief. Oral argument was not requested.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

***ISSUE***

Whether the Administrative Law Judge correctly concluded that the auditor's calculation of additional tax due for 1983 lacked a rational basis.

***FINDINGS OF FACT***

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Petitioners, Charalambos Ballis and Paraskevi Ballis, filed a New York State joint income tax return for 1983 in March of 1984. In that return they reported joint income in the amount of \$17,404.00. Attached to the return were W-2 forms confirming that Mrs. Ballis earned \$10,400.00 from STA Parking Corporation and \$1,300.00 from Hara Foods, Inc., and that Mr. Ballis earned \$1,554.00 from STA Parking Corporation and \$4,150.00 from Hara Foods, Inc. Petitioners did not file a State income tax return for 1984.

Mr. Ballis purchased Hara Foods, Inc. in January of 1983 for \$25,000.00,<sup>1</sup> plus a security deposit of \$5,024.45 to be paid in three monthly installments of \$1,674.85 for a total payment of \$30,024.45. The purchase agreement required a \$5,000.00 payment upon execution of the purchase agreement. Essentially, Mr. Ballis purchased a leasehold and certain fixtures and equipment of a luncheonette/restaurant in which Mr. Ballis thereafter worked as the cook and his wife handled customers.

At some point after the purchase, Mr. and Mrs. Ballis became stockholders in Hara Foods, Inc., each owning 10 shares of the 20 shares of common stock in the business. Petitioners sold their 20 shares of stock for \$70,000.00 in October of 1984. According to the stock purchase agreement, the purchasers were to pay petitioners a \$5,000.00 payment on November 1, 1984,

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<sup>1</sup>In the Division's proposed Finding of Fact "2", it stated that paragraph 2 of the purchase agreement stated a purchase price of \$28,000.00. Although the \$28,000.00 was typed in as the purchase price, this amount was crossed out and replaced in handwritten form with the total purchase price of \$25,000.00.

December 1, 1984 and January 1, 1985, respectively, and 60 payments in the amount of \$1,168.59 commencing November 1, 1984 and then monthly thereafter.

In 1987, the Division of Taxation and Finance ("Division") conducted an audit of petitioners' 1983 and 1984 personal income tax returns. This audit followed from the Division's audit of Hara Foods, Inc. In an affidavit, the Division's auditor explained the reason for the audit as follows:

I believed that these taxpayers underreported their tax liability based upon the fact that for the tax year 1983, the taxpayers reported income of \$17,404, however, in January of 1983, the taxpayers purchased a luncheonette for approximately \$30,000. Immediately, I could not comprehend how someone could buy a business for \$30,000 at the beginning of 1983 and report only \$17,404 in income. Accordingly, I began an audit of these taxpayers and requested certain documentation in order to verify their filed tax returns.

The auditor determined that because he did not receive from the taxpayers sufficient information to verify the accuracy of the 1983 tax return, he conducted an indirect audit<sup>2</sup> to determine petitioners' personal living expenses for the years 1983 and 1984. The auditor based his estimates on bank statements provided by petitioners and information from the Federal Bureau of Labor Statistics concerning the annual costs for a four-person family for the years 1983 and 1984. In his affidavit, the auditor stated that he could no longer find a copy of the information from the Federal Bureau of Labor Statistics on which he relied for his estimates. Instead, he provided a copy of the tables for the years 1980, 1981 and 1982 from the Federal Bureau of Labor Statistics.

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<sup>2</sup>In his workpapers, the auditor referred to this indirect method as the "source and application of funds."

For 1983, the auditor reconstructed petitioners' living expenses. Included in his estimates was the amount of expenses reported by petitioners in their 1983 tax return such as mortgage payments, taxes, medical expenses and contributions. The auditor added to the reported expenses of \$13,203.00 the following amounts allegedly based on tables from the Federal Bureau of Labor Statistics:

Food	\$ 5,600.00
Utilities	3,200.00
Repairs and maintenence	375.00
Transportation	720.00
Clothing	1,000.00
Personal care	550.00
Other Family consumption	1,400.00
Vacations	<u>2,500.00</u>
Total	\$15,345.00

In the copy of the tables from the Federal Bureau of Labor Statistics ("FBLs") for 1980, 1981 and 1982, the following annual costs for a lower level budget family of four in New York City were set forth as follows:

	<u>Food</u>	<u>Auto</u>	<u>Non-auto</u>	<u>Clothing</u>	<u>Personal Care</u>	<u>Other Family Consumption</u>
1980	\$4,651	\$1,654	\$ 969	\$832	\$362	\$644
1981	4,956	1,829	1,087	827	387	701
1982	5,253	1,939	1,152	877	410	743

A comparison between the FBLs tables for the lower budget level family of four and the intermediate budget level family of four for 1982 shows the following:

	<u>lower budget level</u>	<u>intermediate budget level</u>
Food	\$5,253.00	\$6,973.00
Auto owners	1,939.00	
Non-auto	1,152.00	

Transportation		2,707.00
Clothing	877.00	1,261.00
Personal care	410.00	549.00
Other family consumption	743.00	1,374.00
Housing	2,964.00	
Homeowner		7,120.00
Renter		3,533.00

The Federal Bureau of Labor Statistics' tables had no separate categories for "utilities", "repairs and maintenance" or for "vacations". Estimates under these categories, however, were included in the auditor's workpapers in determining petitioners' living expenses.

The auditor also added to the reported and estimated expenses costs with respect to the purchase of Hara Foods, Inc. such as the \$25,000.00 purchase price, \$5,000.00 security deposit, \$2,500.00 in estimated legal fees, and \$1,250.00 in estimated broker's fees. The total amount of income estimated for petitioners for 1983 was \$62,323.00. Subtracting out the \$17,404.00 of reported income, the auditor found unreported income for 1983 in the amount of \$44,919.00 and a State and City income tax deficiency in the amount of \$7,377.77. The auditor determined that because the understated income was more than 25% of New York State adjusted gross income, the tax deficiency could be assessed within six years after the 1983 return was filed under Tax Law § 683(d)(1).

For 1984, the auditor estimated petitioners' living expenses based on bank statements<sup>3</sup> and his estimated personal expenses for 1983 (\$15,345.00) increased by 10% for inflation. To

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<sup>3</sup>Petitioners had a checking account with Manufacturers Hanover Trust. The Division submitted into the record bank statements beginning with the period November 19, 1983 and ending with the period January 1985.

that amount, he added long-term capital gain of \$20,000.00<sup>4</sup> with respect to petitioners' sale of the stock in Hara Foods, Inc. in 1984. In the workpapers, the auditor noted that as of September 23, 1987, petitioners did not file a return as requested and did not make an election for the installment sale.

The workpapers showed that petitioners deposited \$20,802.90 in their bank account throughout 1984. Ultimately, the auditor found estimated unreported income of \$39,081.00 with taxable income of \$30,696.00 for 1984,<sup>5</sup> resulting in a State tax deficiency of \$4,185.99 and a City tax deficiency of \$1,547.17. To this amount, the auditor added penalties under Tax Law § 685(a)(1) for failure to file a tax return, Tax Law § 685(b) for negligence, and Tax Law § 685(a)(2) for failure to pay tax shown on a return. The penalties under Tax Law § 685(a)(2) amounted to \$627.90 and \$232.08, respectively, for State and City tax deficiencies.

The Division issued to petitioners a Notice of Deficiency, dated December 28, 1987, for income tax due for 1983 and 1984 in the amount of \$13,110.93, plus a \$2,891.48 penalty and \$4,121.98 in interest, for the total amount of \$20,129.39.

The Division issued to petitioners four notices and demands, dated May 6, 1988, as follows:

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<sup>4</sup>In the workpapers, the auditor miscalculated the capital gain by subtracting the purchase price of \$25,000.00 from the sale price of \$70,000.00 to arrive at the sum of \$50,000.00 when the sum should have been \$45,000.00. Thus, the correct gain is 40% of \$45,000.00 or \$18,000.00.

<sup>5</sup>The auditor subtracted from the unreported income of \$39,081.00 estimated itemized deductions of \$5,985.00 and three exemptions in the amount of \$2,400.00.

<u>Assessment No.</u>	<u>Year</u>	<u>Amount</u>	<u>Penalty</u>	<u>Add.pen./int.</u>	<u>Total</u>
A8710044021	1983	\$5,509.94	\$ 275.50	\$288.77	\$8,013.32
A8710044022	1983	1,867.83	93.39	97.90	2,716.47
A8710044023	1984	4,185.99	1,779.05	345.02	7,244.77
A8710044024	1984	1,547.17	657.55	127.52	2,677.72

In 1991, the Division levied petitioners' bank accounts to collect the tax owed. At hearing, the Division submitted two checks indicating payments on the levies in the amounts of \$16,713.23 and \$6,697.42 from petitioners' account with Manufacturers Hanover. In a letter dated January 26, 1993 to the Division, petitioners alleged that the Division levied on two savings accounts in 1991 withdrawing all of their savings which aggregated almost \$46,000.00. The Division's counsel stated at the hearing that although the two checks constituted the only evidence she had of collection, petitioners had been levied twice that amount, and therefore, the only issue in dispute involved petitioners' underreporting.

Petitioners filed a claim for credit or refund of personal income tax for 1983 in the amount of \$7,377.77, plus penalty and interest, and a claim for credit or refund for 1984 in the amount of \$5,733.16, plus penalty and interest. In both claims, petitioners stated that they did not have any income for 1984 and therefore, filed "a form showing zero", and that they were not aware of any audit until 1987 when they received the notice of deficiency, which they appealed by petition in November 1987.

By Notice of Disallowance dated January 14, 1993, the Division denied petitioners' refund requests stating that petitioners did not substantiate their claims.

In June of 1995, a conciliation conferee in the Division's Bureau of Conciliation and Mediation Services issued to petitioners a conciliation order sustaining the Notice of Disallowance.

Mr. and Mrs. Ballis filed a petition, dated July 10, 1995, stating:

We submitted copies of Income Tax returns for 1983 showing no income for the entire year and for 1984 showing that we never realized any capital gains from the sale of HARA FOODS, INC.<sup>6</sup>

The Division filed an answer, dated September 13, 1995, affirmatively stating that petitioners' 1983 tax return failed to accurately reflect their State and City taxable income; that petitioners failed to file a 1984 State and City tax return; that on October 24, 1991, the Division levied two of petitioners' bank accounts in the amounts of \$16,713.23 and \$6,697.42; and that petitioners have the burden of proving the tax deficiencies were erroneous.

At the commencement of the hearing held on April 23, 1996, the parties stated the issues in the case. Essentially, the Division's counsel explained how the audit was conducted and concluded that the issue was simply a case of underreporting of income. The Division's counsel stated that:

[o]bviously, the taxpayers lived somewhere, had to eat, had to get back and forth from work, had clothing expenditures, had income other than the \$17,000 that was reported on the income tax return. (Tr. p.19.)

Petitioners' representative stated:

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<sup>6</sup>Although petitioners implied in their statement that they had filed a 1984 tax return, at hearing Mr. Ballis testified that he did not file a 1984 return because he did not have any income in 1984. In addition, in the field audit report, the auditor noted that petitioners filed a timely 1983 tax return but no tax return for 1984. He therefore recommended in that report penalties only for failure to file a tax return under Tax Law § 685(a)(1) and for negligence under Tax Law § 685(b).

First of all, the only -- we thank [the Division's counsel] with providing us with all this additional information. This is the first time we've seen that, except the notice of assessment that was issued in September '87 which we actually receive it in '91. We didn't have any idea why they making these assessments. . . . Now I have a clear picture from the affidavit of . . . the auditor.

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[B]ecause before we file petitions but we didn't have any idea for which reason the assessments were made so we don't know exactly what we're talking about. Now, based on this information, we know exactly and we have some explanation for that. (Tr. pp. 15-16.)

At hearing, Mr. Ballis testified that in 1983 he borrowed from his two brothers-in-law, Constantinos Kessissoglou and George Zacharias, \$15,000.00 each in order to purchase the luncheonette. He explained the origin of the \$30,000.00 as follows:

That wasn't money from my pocket to report that I made. The money, that is what they claimed that I had more income than I report. The original income that I reported to the State was \$17,300, and they questioned -- State question me, where you get the \$30,000 to buy the place. So the \$30,000 I borrow from two of my family people. (Tr. p.23.)

In support of his testimony, two post-hearing affidavits were submitted. In an affidavit by George Zacharias, he stated that in January of 1983 he loaned Mr. Ballis \$15,000.00 to purchase the luncheonette and was repaid in 1984. In an affidavit by Ekaterini Kessissoglou, she stated that she and her ex-husband, Constantinos Kessissoglou, loaned \$15,000.00 to Mr. Ballis in January of 1983 and that the loan was subsequently repaid in 1984.

Mr. Ballis testified that after approximately six months of operating the luncheonette, he and his wife sold Hara Foods, Inc.; that he received a \$10,000.00 payment, which he paid over to his two brothers-in-law on the loans, as well as two or three monthly payments, before the

purchasers defaulted on further payments;<sup>7</sup> and that at some point in 1983 he and his wife moved out of their split-level home due to financial hardship to live with his wife's parents.<sup>8</sup>

Mrs. Ballis gave birth to a child in September of 1983. Mr. Ballis further testified that neither he nor his wife attempted to collect unemployment after the business was sold; that neither he nor his wife had employment during 1984; that during the time they lived with his wife's parents they paid no rent and were provided with food; and that the only income they had during 1984 was rental income of approximately \$2,300.00 per month from renting the basement and upstairs of their home.<sup>9</sup> Mr. Ballis explained his ignorance of the tax law as follows:

A. . . . now, for '84 they tell me that I didn't make no tax return. They're right because I don't have any income. The only income I have from the house. I think those things are not income declarable.

Q. How long were you here at that time?

A. I was new. I didn't know. (Tr. p.23.)

When questioned about his living expenses, he responded as follows:

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<sup>7</sup>The Division submitted into the record copies of 41 promissory notes each in the amount of \$1,168.59 and payable to petitioners from May 1, 1986 through October 1, 1989. There is no evidence in the record that these payments were made to petitioners.

<sup>8</sup>Petitioners reported in 1983 interest expenses with respect to the mortgage on their home in the amount of \$6,545.00. In the Division's proposed Findings of Fact "6" and "7", it included petitioners' address and the address of Mrs. Ballis's parents. These addresses were not included in the Findings of Fact because they are irrelevant to the determination. The Division also proposed a finding that petitioners purchased their home in 1983. However, Mr. Ballis testified that he could not remember the exact date of purchase but that he owned the home by 1983. Therefore, this proposed finding is excluded from the determination.

<sup>9</sup>In proposed Findings of Fact "6" and "7", the Division states that petitioners rented out the basement of their house in 1983 and 1984 and received approximately \$2,300.00 rental income a month during 1983 and 1984. Contrary to these statements, it is unclear from the testimony at what point in 1983, petitioners may have received rental income from their home. It appears that petitioners moved out sometime at the end of 1983. However, it is reasonable from this record to assume that they received rental income for the entire year of 1984.

Q. When you were living with your mother-in-law, who paid for the food?

A. Well, my father-in-law and mother-in-law used to take care of those things.

Q. So they took care of all the food?

A. Don't forget, we used to get from the rent and the house; they had the rental from there. So combined all together we lived as a family. As a matter of fact, I had my mother-in-law with me for the rest of the time.

Q. Now where is Woodside [location of petitioners' split-level home] in relation to where the luncheonette was?

A. If you go from Expressway, right in the Expressway, BQE, going down to Brooklyn Bridge, it was right there.

Q. Did you have a car?

A. At that time I had an old car, yes.

Q. And who would have paid the insurance on the car?

A. Just like that time two, \$300 a year.

Q. What about gas?

A. Gas, small car. You don't need much.

Q. Tolls?

A. We don't have no tolls.

Q. What about parking?

A. No parking. You got parking from the luncheonette.

Q. Now, what about clothes, who would buy clothes for the new baby?

A. We tried to do as much as you can. If you don't have, you don't buy; if you have, you buy. (Tr. pp.31-32.)

During the course of the hearing, it became apparent that English is a second language for Mr. Ballis and that in 1983 his residency in the United States was relatively recent.

Petitioners submitted a post-hearing affidavit by Sotiria Haracoglou, Mrs. Ballis's mother, in which she stated that during 1983 petitioners and their child lived with her at her home "at no cost due to his financial hardship."<sup>10</sup>

***THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE***

The Administrative Law Judge noted that although a determination of an income tax deficiency must have a rational basis to be sustained on review, the Division's issuance of a Notice of Deficiency is presumed correct as long as no evidence is introduced to challenge the deficiency. In this proceeding, the Administrative Law Judge concluded that petitioners provided evidence to rebut certain assumptions underlying the audit. At the hearing, although petitioners did not request the auditor to be present in order to pursue inquiries as to the auditor's methodology, the Administrative Law Judge held that the Division was still required to provide evidence that there was a rational basis for its audit conclusions.

The Administrative Law Judge, after reviewing the auditor's calculation of estimated expenditures based on the Federal Bureau of Labor Statistics, concluded that there was no

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<sup>10</sup>In proposed Finding of Fact "6," the Division states that Mrs. Haracoglou's affidavit "implies that petitioners lived with her for the entire 1983 year". This statement constitutes a conclusion of law that is not included in these Findings of Fact. In proposed Finding of Fact "9," the Division states that the address listed on petitioners' bank statements was the same address as Mrs. Haracoglou's home at that time. The bank statements have the same street address as the street address identified in Mrs. Haracoglou's affidavit as her home in 1983. However, the street address in the bank statements has the street located in Woodside, New York whereas Mrs. Haracoglou indicated the street address was located in Maspeth, New York.

rational basis for the auditor's estimate of additional income tax due for 1983. Further, she concluded that petitioners' testimony demonstrated that the \$30,000.00 used to purchase the luncheonette in January 1983 was obtained as a loan from certain relatives. Thus, the Administrative Law Judge concluded that petitioners were entitled to a refund with respect to 1983. However, as to 1984, the Administrative Law Judge concluded that petitioners erroneously failed to file an income tax return for that year. The record indicated that petitioners received rental income and capital gains during 1984. Since petitioners' taxable income for 1984 exceeded the auditor's estimate of additional taxable income for that year, the Administrative Law Judge concluded that petitioners were not entitled to a refund with respect to the deficiency for 1984. The Administrative Law Judge further concluded that petitioners were entitled to a refund with respect to the penalty asserted under Tax Law § 685(a)(2) for 1984 for failure to pay the tax shown on a tax return since they did not file a tax return in 1984.

#### ***ARGUMENTS ON EXCEPTION***

Although both the Division and petitioners filed notices of exception, petitioners' notice of exception was dismissed as untimely (*see, Matter of Ballis*, Tax Appeals Tribunal, November 26, 1997).

In support of its exception, the Division argues that the findings of fact should indicate that petitioners' house was rented during 1983 and 1984 and that petitioners owned a car which they used to commute to work.

The Division argues that the Administrative Law Judge incorrectly concluded that the auditor's calculation of estimated expenditures did not have a rational basis. Since the audit method was never challenged by petitioners, the Division argues that the presumption of

correctness provided by the issuance of the assessment was itself the rational basis for the assessment. The Division argues that if it was required to establish a rational basis for its assessment, it did so by supplying evidence of the audit methodology used and the calculations employed to arrive at the computation of additional tax assessed. The Division asserts that it was petitioners who failed to meet their burden of proof to establish that the assessment was in error. They failed to produce evidence that they had no other source of income in addition to their reported income for 1983.

### ***OPINION***

We disagree with the Administrative Law Judge's conclusion that there was no rational basis for the assessment of additional income tax for 1983. In December 1987, a Notice of Deficiency was issued to petitioners asserting additional income tax due for the years 1983 and 1984. A presumption of correctness was raised by the issuance of the Notice of Deficiency which, in itself, provided the rational basis for the assessment until such time as petitioners introduced evidence challenging the assessment (*Matter of Atlantic & Hudson Ltd. Partnership*, Tax Appeals Tribunal, January 30, 1992). Petitioners did not avail themselves of their ability to challenge the Notice of Deficiency because they did not protest that Notice within the time available to them to do so. Although petitioners allege that they filed a petition in November 1987 protesting the assertion of additional tax, there is no evidence that a timely proceeding for review was commenced in the Division of Tax Appeals. Furthermore, since the Notice of Deficiency was not issued until December 1987, any petition purporting to protest such Notice would have been premature if filed in November 1987 and the Division of Tax Appeals would not have had jurisdiction to entertain it (*Matter of West Mountain v. Department of Taxation &*

*Fin.*, 105 AD2d 989, 482 NYS2d 140, *affd* 64 NY2d 991, 489 NYS2d 62; *Matter of Yegnuikian*, Tax Appeals Tribunal, March 2, 1990).

Once petitioners' time to protest the Notice of Deficiency expired, that Notice became an unchallengeable assessment of additional tax (Tax Law § 681). The rationality of the methodology used by the Division to calculate that assessment ceased to be an issue since petitioners, by not introducing evidence to show the incorrectness of the Notice of Deficiency, surrendered to the presumption of correctness (*Matter of Leogrande v. Tax Appeals Tribunal*, 187 AD2d 768, 589 NYS2d 383, *lv denied* 81 NY2d 704, 595 NYS2d 398).

The present claim for refund is not a challenge to the audit methodology but an assertion that the amount of tax paid exceeded the amount of tax owed for the period at issue. Petitioners bear the burden of proof to show by clear and convincing evidence that they are entitled to a refund (*Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451). To the extent that they have shown that \$30,000.00 of the estimated additional income on which their assessment was premised for 1983 consisted of loan proceeds rather than taxable income, we agree with the Administrative Law Judge that they have met their burden of proof. However, that is the full extent of the proof that petitioners offered to demonstrate entitlement to a refund for 1983. Their satisfactory refutation of additional tax based on their receipt of loan proceeds does not negate the entire assessment for 1983. Thus, petitioners have failed to meet their burden of proof to demonstrate entitlement to a reduction in their tax liability for 1983 beyond the amount thereof attributable to the \$30,000.00 which they obtained by borrowing.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is granted to the extent that petitioners are not entitled to any refund of income tax for 1983 in excess of the amount of tax imposed on \$30,000.00 for that year, but is otherwise denied;

2. The amended determination of the Administrative Law Judge is modified in accordance with paragraph "1" above, but is otherwise sustained;

3. The petition of Charalambos and Paraskevi Ballis is granted to the extent that, for 1983, they are entitled to a refund of income tax paid on \$30,000.00 and, for 1984, they are entitled to a refund of penalties paid under Tax Law § 685(a)(2), but is otherwise denied; and

4. The claim for refund is granted to the extent set forth in paragraph "3" above, but is otherwise denied.

DATED: Troy, New York  
July 2, 1998

/s/Donald C. DeWitt

Donald C. DeWitt  
President

/s/Carroll R. Jenkins

Carroll R. Jenkins  
Commissioner

/s/Joseph W. Pinto, Jr.

Joseph W. Pinto, Jr.  
Commissioner