

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
RAMONA MORALES AND PEDRO D. CHAMORRO :		SMALL CLAIMS DETERMINATION DTA NO. 820639
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 Administrative Code of the City of New York for the Years 1999 and 2000.	:	

Petitioners, Ramona Morales and Pedro D. Chamorro, 2776 Tiemann Avenue, Bronx, New York 10469, filed a petition 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 1999 and 2000.

A small claims hearing was held before Winifred M. Maloney, Presiding Officer, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on July 25, 2006 at 2:30 P.M., with additional documents due by November 3, 2006, which date began the three-month period for the issuance of this determination. Petitioner Ramona Morales appeared *pro se* and on behalf of her husband, Pedro D. Chamorro. The Division of Taxation appeared by Mark F. Volk, Esq. (Yvette Travis and Matthew Roberts).

ISSUE

Whether the Division of Taxation properly determined petitioners' tax liability for the years 1999 and 2000.

FINDINGS OF FACT

1. Petitioners, Ramona Morales and Pedro D. Chamorro, timely filed a New York State resident income tax return for the year 1999. Petitioners' New York adjusted gross income for the year 1999 included the following items of income

ITEM	INCOME
Interest Income	\$ 161.00
Business Income	7,663.00
Other losses (Federal Form 4797)	(385.00)
Rental Real Estate	34,101.00
Adjustments: ½ of s/e tax	<u>(541.00)</u>
New York adjusted gross income	\$40,999.00

After claiming itemized deductions of \$23,503.00 and a dependent exemption of \$1,000.00, petitioners determined their taxable income to be \$16,496.00, their New York State tax to be \$661.00 and their City of New York resident tax to be \$502.00, less a City of NY school tax credit of \$35.00, for total New York State and New York City taxes due in the amount of \$1,159.00.

2. For the year 1999, petitioners reported business income in the amount of \$7,663.00, which was the sum of the profits or losses from five sole proprietorships run by Ms. Morales or Mr. Chamorro. Petitioners reported that Ms. Morales operated the following three businesses as sole proprietorships in 1999: travel arrangements under the business name Tremont Travel Agency (hereafter "Tremont Travel - Ramona"), insurance underwriting under the business name Ceiba Brokerage and income tax preparation under the business name Tremont Travel Agency (hereafter "income tax preparation"). They reported that Mr. Chamorro operated the

following two businesses in 1999: travel arrangement manager under the business name Tremont Travel Agency (hereafter “Tremont Travel - Pedro”) and money transfers under the business name Western Union. A copy of a Federal Schedule C, Profit or Loss From Business, (hereafter “Federal Schedule C”) for each of the businesses was attached to petitioners’ New York State resident income tax return for the year 1999.

3. The Federal Schedules C for Tremont Travel - Ramona and Tremont Travel - Pedro for the year 1999 each reported the following items of income and expenses:

	Tremont Travel - Ramona	Tremont Travel - Pedro
Gross receipts	\$1,490,911.00	\$30,000.00
less: Returns and allowances	1,368,213.00	0.00
less: Cost of goods sold	0.00	0.00
Gross income	125,698.00	30,000.00
Less: Advertising	2,300.00	985.00
Bad debts	3,500.00	0.00
Car and truck expenses	0.00	4,770.00
Employee benefit programs	728.00	0.00
Insurance	1,515.00	12,890.00
Interest: Mortgage	789.00	0.00
Legal and professional services	350.00	500.00
Office expense	855.00	2,545.00
Vehicle lease	950.00	3,300.00
Repairs and maintenance	550.00	300.00
Supplies	3,300.00	0.00
Taxes and licenses	850.00	0.00
Travel, meals and entertainment	1,500.00	1,290.00
Wages	79,255.00	0.00

Utilities	0.00	259.00
Other: Con Ed	3,200.00	0.00
Other: Rent	21,300.00	0.00
Other: Garbage disposal	576.00	0.00
Other: Working clothes	0.00	2,345.00
Other: Working clothes Upkeep	450.00	0.00
Total expenses	122,018.00	29,184.00
Net Profit	\$3,680.00	\$816.00

4. On the Federal Schedule C for Ceiba Brokerage for the year 1999, the insurance underwriting business run by Ms. Morales, petitioners reported gross income in the amount of \$19,914.00, expenses totaling \$19,914.00, consisting of advertising expenses of \$2,890.00, bad debts of \$550.00, office expenses of \$1,350.00 and other expenses, i.e., administrative fees, of \$15,214.00, and a net profit (loss) in the amount of zero dollars. On the Federal Schedule C for Ms. Morales's income tax preparation business conducted under the name Tremont Travel Agency for the year 1999, petitioners reported gross income in the amount of \$8,360.00, expenses totaling \$5,140.00, consisting of advertising expenses of \$780.00, commissions and fees of \$400.00, office expense of \$700.00, utilities of \$650.00, and other expenses totaling \$2,610.00 (consisting of a tax program in the amount of \$790.00, transmissions in the amount of \$355.00, supplies in the amount of \$425.00, toner and maintenance in the amount of \$950.00, and envelopes in the amount of \$90.00), and a net profit in the amount of \$3,220.00.

5. On the Federal Schedule C for Mr. Chamorro's operation of a money transfer business, conducted under the name Western Union, for the year 1999, petitioners reported gross income in the amount of \$5,809.00, expenses totaling \$5,862.00, consisting of bad debts of \$430.00, legal and professional services of \$250.00, office expenses of \$450.00, repairs and maintenance

of \$156.00, supplies of \$300.00, utilities of \$276.00 and other expenses, i.e., loan repayment, in the amount of \$4,000.00, and a net loss in the amount of \$53.00.

6. On or about May 9, 2002, the Division of Taxation (the “Division”) assigned Yvette Travis to conduct a field audit of petitioners’ New York State resident income tax returns for the years 1999 and 2000. A review of the Income Tax Report of Audit (“audit report”) prepared by Ms. Travis indicates that the initial focus of the Division’s field audit was on various Schedule C businesses conducted by petitioners in the years 1999 and 2000.

7. In letters dated May 9, 2002, June 7, 2002 and July 9, 2002, the auditor requested the following documentation from petitioners: copies of their Federal and State income tax returns for the years 1999 and 2000; all books, records, worksheets, schedules and other documents pertinent to the preparation of their tax returns; bank statements for business and personal checking and saving accounts; canceled checks and statements for brokerage accounts for the years 1999 and 2000; purchase and sales invoices related to their businesses for the years 1999 and 2000 and substantiation for expenses which they claimed on each Schedule C.

8. After petitioners failed to respond the Division’s third request for information, the auditor prepared statements of personal income tax audit changes for the years 1999 and 2000 dated August 12, 2002 and sent them to petitioners. A review of the Tax Field Audit Record (“audit record”) indicates that all expenses reported on schedules C, E and A were disallowed for lack of substantiation in the Statement of Personal Income Tax Audit Changes which the auditor prepared for the year 1999. Further review of the audit record indicates that the audit adjustments set forth in the Statement of Personal Income Tax Audit Changes for the year 2000 were based on an average of the years 1998 and 1999 because petitioners had not filed a New York State resident income tax return for the year 2000.

9. Entries in the audit record reveal that, shortly after receiving both statements of personal income tax audit changes, petitioners began submitting some documentation for the auditor to review. As a result of her review of the documents submitted, the auditor made additional requests for information, including documentation previously requested. Subsequent entries in the audit record indicate that petitioners, over an extended period of time, supplied a portion of the requested documentation, including documentation to substantiate some expenses claimed on their tax return for the year 1999, some bank statements and some documentation for the year 2000.

10. On November 27, 2002, petitioners executed a consent extending the period of assessment of personal income tax for the year 1999 until April 15, 2004.

11. On or about February 25, 2003, the auditor prepared statements of personal income tax audit changes for the years 1999 and 2000. Notations in the audit record indicate that the two statements were sent to petitioners along with supporting schedules showing allowed and disallowed expenses for the year 1999 and a letter explaining the source of the audit adjustments for the year 2000. On March 26, 2003, the auditor received a letter from Ms. Morales in which she stated that she did not understand how the Division arrived at the figures set forth in the statements of personal income tax audit changes and was hiring a certified public accountant to review the audit.

12. On May 12, 2003, the Division received the power of attorney executed by petitioners appointing Anthony Raymond, CPA, as their representative with respect to the income tax returns for the years 1999 and 2000.

13. By letter dated May 20, 2003, petitioners' representative advised the auditor that Ceiba Brokerage should not be included in the determination of petitioners' personal income tax

liabilities because Ceiba Brokerage Corp. was a duly filed New York State corporation. In this letter, the representative also requested that petitioners be allowed to amend their personal income tax returns and to file properly prepared corporation tax returns. A copy of the New York State Department of State filing receipt for Ceiba Broker Corp.'s incorporation was enclosed with the letter.

14. In a letter to petitioners' representative dated May 21, 2003, the auditor set a deadline of June 20, 2003 for the submission of all amended returns. On June 24, 2003, the auditor sent a final notice letter to petitioners' representative in which a deadline of July 8, 2003 was set for the submission of all amended returns.

15. On or about July 16, 2003, petitioners submitted amended personal income tax returns for the years 1999 and 2000, but failed to submit Ceiba Brokerage Corp.'s income tax returns. Based on her review of the amended returns, the auditor sent petitioners' representative a letter dated July 16, 2003 requesting an explanation of the Federal adjusted gross income figure of \$977.00 reported on the amended return for the year 2000 and the submission of general business corporation franchise tax return short forms (forms CT-4) for Ceiba Brokerage Corp. by July 31, 2003. This letter also informed petitioners' representative that the "amended returns are not final" because "various adjustments to Schedule A and Schedule Cs" were not reflected in the amended returns submitted by petitioners. A worksheet of the various adjustments was attached to the letter. A second notice letter dated August 5, 2003 was sent to petitioners' representative setting a deadline of August 18, 2003 for the submission of the documents requested previously in the July 16, 2003 letter. On August 28, 2003, the auditor received copies of Ceiba Brokerage Corp.'s income tax returns prepared by petitioners' representative for the years 1999 and 2000 from Ms. Morales. No additional substantiation was submitted.

16. Based on her review of the documentation submitted by petitioners related to their income and expenses for the year 1999, the auditor made the following audit adjustments:

a. disallowed all income and expenses reported on the Schedule C for the Western Union (money transfer) business, resulting in an increase of \$53.00 to New York State income;

b. disallowed expenses totaling \$2,560.46, consisting of insurance expense in the amount of \$197.19, rent or lease expense in the amount of \$1,800.00, garbage disposal (other expense) in the amount of \$113.28 and working clothes (other expense) in the amount of \$450.00, reported on the Schedule C for the Tremont Travel - Ramona business, resulting in an increase of \$2,560.00 to New York State income;

c. disallowed all expenses, i.e., \$29,184.00, reported on the Schedule C for the Tremont Travel - Pedro business and added additional income in the amount of \$39,812.00, which amount consisted of unreported income from bank statements plus the sum of the receipts from the Western Union (money transfer) and income tax preparation businesses, to Tremont Travel - Pedro, resulting in an increase of \$68,996.00 to New York State income;

d. disallowed all income and expenses associated with the Schedule C income tax preparation business, resulting in a decrease to New York State income in the amount of \$3,220.00;

f. the auditor disallowed the Ceiba Brokerage Schedule C because it was a corporation and filing a Schedule C was not permitted. However, no adjustment was necessary to New York State income because petitioners reported net income of zero dollars on the Ceiba Brokerage Schedule C for 1999 and

g. the auditor also disallowed \$2,894.00 in mortgage interest claimed as an itemized deduction.

The auditor's adjustments to the income and expenses of the various Schedule C businesses, i.e, \$71,609.00 in total increases to New York State income less \$3,220.00 in total decreases to New York State income, resulted in a \$68,389.00 net increase in petitioners' New York State income for the year 1999. After disallowing \$2,894.00 in itemized deductions, the auditor determined New York adjusted itemized deductions, before modification, to be \$20,609.00 for the year 1999. The auditor did not make any further modifications to the New York adjusted itemized deductions determined for the year 1999.

17. On October 1, 2003, the Division issued a Final Statement of Personal Income Tax Audit Changes to petitioners asserting additional New York State and New York City personal income taxes due in the amount of \$7,311.00, plus penalties and interest, for a total amount due of \$11,471.00 for the year 1999. This Statement of Personal Income Tax Audit Changes reflected the auditor's inclusion of additional unreported business income from bank statements and her disallowance of Schedule C items of income and expenses and Schedule A itemized deductions because of lack of substantiation, which audit adjustments are outlined above.

The Statement of Personal Income Tax Audit Changes for the year 1999 contained a corrected tax computation as follows. New York State adjusted gross income per return in the amount of \$40,999.00 was increased by a total of \$68,389.00 and the corrected adjusted gross income was determined to be \$109,388.00. Corrected itemized deductions of \$20,609.00 and a \$1,000.00 dependent exemption were subtracted from the corrected adjusted gross income of \$109,388.00 resulting in corrected New York State taxable income in the amount of \$87,779.00, a recomputed New York State tax liability in the amount of \$5,368.00, less tax previously paid in the amount of \$661.00, for an additional New York State tax liability due in the amount of \$4,707.00 and a corrected New York City tax liability of \$3,071.00 (recomputed New York City

tax liability of \$3,106.00 less a total of \$70.00 in New York City other tax credits) less tax previously paid in the amount of \$502.00, for an additional New York City tax liability due in the amount of \$2,604.00. In addition to the tax asserted to be due, the Division imposed penalties pursuant to Tax Law § 685(b)(1) and (2) for negligence and Tax Law § 685(p) for substantial understatement of liability.

18. For the year 2000, based on information she obtained from documents provided by petitioners and their Federal income tax return, the auditor determined petitioners' corrected New York State adjusted gross income to be \$84,267.00, consisting of the following items of income:

- a. net income from money transfers and income tax preparation business in the amount of \$9,481.00;
- b. net income generated by Tremont Travel - Ramona (Schedule C) in the amount of \$3,778.00;
- c. income from Allstate insurance commissions in the amount of \$2,839.00;
- d. rental real estate net income (Schedule E) in the amount of \$14,143.00;
- f. gain on sale of home in the amount of \$31,026.00 and
- g. net income from Tremont Travel - Pedro (Schedule C) in the amount of \$23,000.00.

The auditor did not include income from Ceiba Brokerage Corporation in her calculation of petitioners' corrected New York State adjusted gross income for the year 2000.

19. Itemized deductions in the amount of \$15,868.00, consisting of medical expenses in the amount of \$4,684.00; taxes in the amount of \$4,838.00; mortgage interest in the amount of \$3,796.00 and gifts to charity in the amount of \$2,550.00, were allowed by the auditor for the

year 2000. The auditor did not make any further modifications to the corrected New York itemized deductions determined for the year 2000.

20. On October 1, 2003, the Division issued a Final Statement of Personal Income Tax Audit Changes to petitioners asserting additional New York State and New York City personal income taxes due in the amount of \$6,083.00, plus penalties and interest, for a total amount due \$9,402.00 for the year 2000. This Final Statement of Personal Income Tax Audit Changes reflected the auditor's determination of various items of petitioners' income and expenses, as outlined above, based on documents provided and their Federal income tax return for the year 2000 because they failed to file a New York State resident income tax return for the year 2000.

The Final Statement of Personal Income Tax Audit Changes for the year 2000 contained a corrected tax computation as follows. Based on audit adjustments to New York State income, the corrected New York State adjusted gross income was determined to be \$84,267.00. Corrected New York itemized deductions in the amount of \$15,868.00 and a \$1,000.00 dependent exemption were subtracted from the corrected New York State adjusted gross of \$84,267.00 resulting in a corrected New York State taxable income in the amount of \$67,399.00, a recomputed New York State tax liability due in the amount of \$3,823.00 and a corrected New York City tax liability due in the amount of \$2,175.00 (recomputed New York City tax liability in the amount of \$2,260.00 less New York City other tax credits totaling \$170.00). In addition to the tax asserted to be due, the Division imposed penalties pursuant to Tax Law § 685(a)(1) for failure to file a return and Tax Law § 685(b)(1) and (2) for negligence.

21. After receiving the final statements of personal income tax audit changes for the years 1999 and 2000, petitioners' representative left the auditor a voice mail message requesting the opportunity to discuss the audit findings. Entries in the audit record indicate that the auditor and

the representative had a number of telephone conversations concerning the proposed audit adjustments reflected in the final statements. Further review of the audit record indicates that petitioners' representative was given additional time to submit substantiation concerning adjustments made to items of petitioners' income and expenses for both years.

22. Despite repeated oral assurances by petitioners' representative that additional documentation would be submitted, no further documentation was submitted prior to the issuance of the Notice of Deficiency at issue in this proceeding.

23. Subsequently, the Division issued to petitioners a Notice of Deficiency (Notice No. L-023396250-5), dated January 2, 2004, asserting additional New York State and New York City personal income taxes due in the total amount of \$13,394.00 for the years 1999 and 2000, plus interest of \$3,113.97 and penalties of \$4,684.48, for a current amount due of \$21,192.45. The computation section contained the following explanation: "[f]ield audit of your records disclosed additional tax due."

24. Petitioners requested a conciliation conference which was held on January 12, 2005. After the conciliation conference, the conferee issued a Conciliation Order (CMS No. 201943), dated March 25, 2005, which denied the request and sustained the Notice of Deficiency.

25. On July 22, 2005, petitioners filed a petition with the Division of Tax Appeals seeking a redetermination of the deficiency for the years 1999 and 2000. In their petition, petitioners alleged that the conciliation conference took place despite their requests for a third postponement, but there was no review of the audit findings because they did not submit documentation at that conference. They further alleged that they were unable to submit documentation at the conciliation conference because the Internal Revenue Service ("IRS") had not completed its audit review of the same tax years at that time. In their petition, petitioners

asserted that they would be able to provide documentation to substantiate their protest at the small claims hearing.

26. In its answer, the Division raised the timeliness of the filing of the petition with the Division of Tax Appeals. However, the Division later found that its proof of mailing of the Conciliation Order was not sufficient and notified the Division of Tax Appeals and petitioners of that fact in a letter dated June 8, 2006. The small claims hearing held on July 25, 2006 addressed petitioners' challenge of the Division's determination that additional New York State and New York City personal income taxes were due for the years 1999 and 2000.

27. At the small claims hearing, petitioners requested that their New York State and New York City personal income tax liabilities for the years 1999 and 2000 be recomputed based upon the IRS's audit determination of taxable income for both years.

28. On an unknown date, the IRS began an audit of petitioners' Federal income tax returns for the years 1999 and 2000. After examining petitioners' books and records and meeting with Ms. Morales approximately seven times, the revenue agent made audit adjustments to petitioners' Federal income tax returns for tax years 1999 and 2000, and a Form 4549B Income Tax Examination Changes ("Federal audit report") was issued for both years. Based on petitioners' challenge of the Federal audit report findings for both years, further audit adjustments were made and corrected Federal audit reports were issued for both years. Petitioners appealed the findings in the corrected Federal audit reports for both years and after an appeals hearing, additional audit changes were recommended. However, at the time of the small claims hearing, the final Federal audit determinations had not been issued for either 1999 or 2000.

29. At the small claims hearing, petitioners submitted copies of the corrected Federal audit reports for years 1999 and 2000, a copy of a check payable to Ramona Morales in the amount of \$50,000.00 which was used as the deposit for petitioners' purchase of three residential rental properties, i.e., numbers 866, 867 and 868 East 164th Street, Bronx, New York, and a copy of the Federal audit report issued for the years 1999 and 2000 by the first auditor, to which an incomplete copy of a Form 886-A Explanations Of Items, prepared by the auditor as supporting documentation for the Federal audit report, was attached. Additional time was given for petitioners' submission of, among other things, copies of their Federal income tax returns for the years 1999 and 2000, copies of the three amended Federal income tax returns filed for the year 1999, copies of the two amended Federal income tax returns for the year 2000 and copies of the final Federal audit adjustments for the years 1999 and 2000.

30. Post-hearing, petitioners submitted additional documents including, *inter alia*, a copy of the IRS tax return transcript for the year 2000 and a copy of a letter dated August 24, 2006 from Norbert Fernandez, a case advocate in the IRS's Taxpayer Advocate Service New York, New York offices.

31. A review of the case advocate's August 24, 2006 letter to Ms. Morales indicates that examination results for the year 1999 were presently being processed and, on August 10, 2006, a collection hold was placed on petitioners' 2000 tax account for up to 12 weeks pending final determination. Further review of the letter indicates that the case advocate was going to address petitioners' concerns about the tax adjustments for the years 1999 and 2000 and determine if audit reconsideration was appropriate.

32. Although petitioners were given the opportunity to request additional time to submit the final Federal audit changes for the years 1999 and 2000, they did not do so and the record closed on November 3, 2006.

33. Documentation in the record indicates that, in addition to the sale of petitioners' unidentified main home on January 30, 2000, petitioners sold two residential rental properties in the year 2000, to wit: 866 East 164th Street, Bronx, New York and 867 East 164th Street, Bronx, New York, but failed to report gains from the two residential rental property sales on the New York State income tax return for the year 2000 which they submitted to the auditor during the audit.

CONCLUSIONS OF LAW

A. Tax Law § 681(a) provides, in pertinent part, as follows:

If upon examination of a taxpayer's return under this article the tax commission determines that there is a deficiency of income tax, it may mail a notice of deficiency to the taxpayer. If a taxpayer fails to file an income tax return required under this article, the tax commission is authorized to estimate the taxpayer's New York taxable income and tax thereon, from any information in its possession, and to mail a notice of deficiency to the taxpayer.

B. In the instant matter, the Division commenced its audit of petitioners' New York State personal income tax returns for the years 1999 and 2000 on May 9, 2002 and initially focused on the various Schedule C businesses conducted by petitioners during those years. The record indicates that the Division made numerous written and oral requests for documentation necessary for both the substantiation of items of income and expenses reported on petitioners' New York State personal income tax return for the year 1999 and the determination of petitioners' New York State and New York City personal income tax liabilities for the year 2000. The record further indicates that petitioners submitted some, but not all, of the requested documentation for both years in a piecemeal fashion over an extended period of time. After reviewing the

submitted documentation which included bank statements, the auditor determined that petitioners had unreported business income and failed to substantiate expenses claimed on various Schedules C and Schedule A for the year 1999. Subsequently, a Statement of Personal Income Tax Audit Changes for the year 1999 was issued based upon that determination. With respect to the year 2000, since petitioners had not filed a New York State resident income tax return prior to the commencement of the audit, the auditor used documents provided by them and their Federal income tax return to determine petitioners' New York State and New York City personal income tax liabilities. Subsequently, a Statement of Personal Income Tax Audit Changes for the year 2000 was issued based upon that determination. Although they were given the opportunity to submit further documentation in response to the statements of personal income tax audit changes for the years 1999 and 2000, petitioners failed to do so and the subject Notice of Deficiency was issued. Pursuant to Tax Law § 681(a), the Notice of Deficiency was properly issued for the years at issue.

C. Where, as here, the Division properly issued a Notice of Deficiency to a taxpayer, a presumption of correctness attaches to such notice (*see, Matter of Land Transport Corporation*, Tax Appeals Tribunal, June 29, 2000; *Matter of Atlantic & Hudson Ltd. Partnership*, Tax Appeals Tribunal, January 30, 1992). In proceedings for review of a properly issued notice of deficiency, the burden of proof is on the taxpayer to demonstrate that the deficiency assessment is erroneous (Tax Law § 689[e]).

D. In the instant matter, the Division determined that additional New York State and New York City personal income taxes were due for the years 1999 and 2000 based upon documentation submitted by petitioners during the audit. As noted, in arriving at its determination that additional New York State and New York City personal income taxes were

due for the year 1999, the Division determined that petitioners had additional unreported business income and failed to substantiate certain expenses associated with various Schedule C businesses and certain Schedule A itemized deductions. With respect to the year 2000, the Division used documentation provided by petitioners and their Federal income tax return to determine items of income, allowable deductions and dependent exemption, and the amount of New York State and New York City personal income tax due for year 2000 because petitioners had not filed a New York State personal income tax return for that year prior to the commencement of the audit.

At the small claims hearing, petitioners requested that their New York State and New York City personal income tax liabilities for the years 1999 and 2000 be recomputed based upon the IRS's audit determination of taxable income for both years and the Notice of Deficiency at issue be adjusted accordingly. In support of this request, petitioners submitted, among other things, a copy of the original Federal audit report for the years 1999 and 2000, copies of the corrected Federal audit reports for the years 1999 and 2000, a copy of the IRS tax return transcript for the year 2000 and copies of amended tax returns for the years 1999 and 2000. It is noted that petitioners failed to submit copies of the IRS revenue agent's supporting explanations which detail the items of income and expense both before and after the audit adjustments, the amount of the audit adjustments and the rationale for the Federal audit adjustments for the years 1999 and 2000. Despite petitioners' claims that supporting explanations of the audit changes did not accompany the Federal audit reports which they received from the IRS, an incomplete copy of the supporting explanation of audit changes made by the original IRS revenue agent is part of the record. Petitioners did not submit a copy of the final Federal audit determination for either year at issue. Rather, they submitted correspondence which appears to indicate that final Federal

audit changes for the years 1999 and 2000 might be issued sometime in the future. However, the same correspondence also indicates that further review of those audit changes might be recommended by the IRS's Taxpayer Advocate Service case advocate assigned to assist petitioners in their appeal of the IRS's audit determinations for the years 1999 and 2000. Given the limited and incomplete documentation submitted by petitioners concerning the IRS's audit of their Federal income tax returns for the years 1999 and 2000, I find that petitioners have failed to sustain their burden of proof (Tax Law § 689[e]). The lack of any additional underlying source documentation makes it impossible for me to determine if any of petitioners' items of income and associated expenses for either 1999 and 2000 should be adjusted. Therefore, I find that no adjustment to the Division's determination of petitioners' income and expenses and recomputation of tax for either 1999 and 2000 is warranted.

E. Tax Law § 659 provides that if the amount of a taxpayer's Federal taxable income reported on his Federal income tax return for any taxable year is changed or corrected, the taxpayer shall report the change or correction within 90 days after the final determination of such change or correction. Immediately upon their receipt of the final Federal audit changes for the years 1999 and 2000, petitioners should report the final Federal audit changes for those years to the Division. Once it has had the opportunity to review the reported final Federal audit changes for the years 1999 and 2000, the Division may find that adjustments to the tax liabilities assessed in Notice of Deficiency are appropriate.

F. The petition of Ramona Morales and Pedro D. Chamorro is denied and the Notice of Deficiency dated January 2, 2004 is sustained.

DATED: Troy, New York
February 1, 2007

/s/ Winifred M. Maloney
PRESIDING OFFICER