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1959, 1960 and 1961, respectively. In addition to deficiency assessments, the report proposed penalties for failure to pay estimated income tax and for fraud. The audit report contains schedules which indicate the specific amounts and computation methods used to obtain the above **corrected** taxable income figures.

Appellant and Mr. Meyer accepted the Service's audit report and the federal taxes and penalties were, **subsequently** paid. Mr. Tuchinsky now states that he was extremely ill when the report was presented to him and he did not have the strength nor the funds to contest the federal action. Appellant states that the Internal Revenue Service took all of his books and records and has not returned them. Mr. Tuchinsky has submitted his own computations, based upon memory, which indicate that the business suffered net losses of **\$5,529.99** and **\$8,038.24** for 1959 and 1960, and a net profit of **\$2,164.05** for 1961.

These computations differ in three specific aspects from the calculations contained in the federal audit report. Appellant has computed substantially lower gross profit on sales figures by **dividing total sales** amounts into estimated annual liquor, tobacco, and "other" sales figures, and then applying an estimated profit percentage to each classification. A significantly larger wage deduction has been calculated from the **employment taxes shown** on the federal report. Mr. Tuchinsky argues that this larger figure is consistent with his statement that there were three full-time employees and one part-time employee during the period in question. An additional license fee deduction is claimed under the assumption that this item was omitted from the Service's computations.

The Franchise Tax Board's proposed assessments were based upon the federal audit report except that Failure to file penalties, pursuant to section 18681 of the Revenue and Taxation Code, were substituted for the failure to pay estimated tax penalties. Whether the deficiency assessments and the failure to file and fraud penalty assessments were correct is the sole issue presented by this appeal.,

Deficiency assessments which are based upon a federal audit report are presumed to be correct and therefore the taxpayer has the burden of proving error. (Appeal of Henrietta Swimmer, Cal. St. Bd. of Equal., Dec. 10, 1963; Anneal of Nicholas H. Obritsch, Cal. St. Bd. of Equal., Feb. 17, 1959.) Appellant's only

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attempt to satisfy this burden has been his submission of computations based, upon his memory. Supporting evidence has not been offered with respect to these figures. Mr. Tuchinsky argues that 'his books and records, allegedly retained by -the Internal Revenue Service, would help his position. Howe'ver, these materials, to the extent that they were found acceptable, were used by the Service in its preparation of the audit report. Also, if appellant 's computations do accurately reflect the business operations in question, there are certainly other accessible sources of supporting evidence .

In addition to this lack of substantiation, appellant's figures contain significant weaknesses. The Franchise Tax Board has properly pointed out the unreliability of Mr. Tuchinsky's estimated profit percentages when the books of, the business were never closed to profit and loss.' That board has also demonstrated that, appellant used an erroneous employment tax percentage to calculate his claimed wage deductions. The deductions allowed, in the federal audit report are much more consistent with the tax percentage level established by respondent . We must conclude that appellant has failed to establish that the deficiency assessments- were inaccurate .

During the years on appeal, the Revenue, and Taxation Code provided:

18401. Every individual taxable under this part shall make a return to the Franchise Tax Board, stating specifically the items of his gross income and the deductions and credits allowed by this part, if he has for the taxable year--

(a) A net income of one' thousand five hundred dollars (\$1,500) or over, if single;

(b) A net income of three thousand dollars" . . . (\$3,000) or over, if married; or

(c) A gross income of five thousand dollars (\$5,000) or over, regardless of the amount of net income .

18402. If a husband' and wife have 'for the taxable year an aggregate net income of three thousand dollars (\$3,000) or over,

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or an aggregate gross income of five thousand dollars (\$5,000) or over--

(a) Each shall make such a return, or

(b) -The income of each shall be included in a single joint return, ..

Section 18681 of the same' code provided in part:

If any taxpayer fails to make and file a return required by this part on or before the due date of the return or the due date as extended by the Franchise Tax Board, then, unless it is shown that the failure is due to reasonable cause and not due to wilful neglect, 5 percent of the tax shall be added to the tax for each 30 days or fraction thereof elapsing between the, due date- of the return and the date on which filed, but the total penalty shall not exceed 25 percent of the tax....

In order to establish reasonable cause, the taxpayer must demonstrate that his failure to file occurred notwithstanding the exercise of ordinary business care and prudence. (Sanders v. Commissioner, 225 F.2d 629, cert. denied, 350 U.S. 967 [100 L. Ed. 839]; Appeal of La Salle Hotel Co., Cal. St. Bd. of Equal., Nov. 23, 1966.)

Appellant has explained that he thought that his net income levels failed to reach the minimums stated in sections 18401 and 18402 of the Revenue and Taxation Code. Certainly such a conclusion does not satisfy the standard of ordinary business care and prudence when it is considered that appellant's books were in very poor condition and were never closed to profit and loss. Furthermore, appellant's computations, -which allegedly are based upon his memory of events during the years in question, indicate gross incomes for these years varying from approximately five to seven and one-half times the \$5,000 minimum amounts stated in sections 18401 and 18402. We conclude that Mr. Tuchinsky has not shown that his failures to file were due to reasonable cause and not due to wilful neglect.

Section 18685 of the Revenue and Taxation Code provides :

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If any part of any deficiency is due to fraud with intent to evade tax, 50 percent of the total amount of the deficiency, in addition to the deficiency and other penalties provided in this article, shall be assessed, collected, and paid in the same manner as if it were a deficiency.

The Franchise Tax Board has the burden of proving fraud by clear and convincing evidence, (Appeal of Robert C. Sherwood, Deceased, and Irene Sherwood, Cal. St. Bd. of Equal., Nov. 30, 1965.) Since direct evidence is seldom available, the existence of fraud usually must be determined from the.. surrounding' circumstances. (Appeals of Leonard S. and Frances M. Gordon, Cal. St. Bd. of Equal., Nov. 14, 1960.)

In the present case, appellant was involved in a business activity which generated average annual sales of approximately \$225,000 during the years in question. However, Mr. Tuchinsky did not maintain adequate records. (Merritt v. Commissioner, 301 F.2d 484; Henrw O. Hart, T.C. Memo., Mar. 1, 1962.) Nor did he close his books to profit and loss, which is a basic' accounting prerequisite to a good faith determination of whether tax liability exists, Appellant wilfully failed to file returns for the period on appeal. (Fred N. Acker, 26 T.C. 107; Herbert C. Broyhill, T.C. Memo., Feb. 14, 1968.) The resulting consistent omission of substantial amounts of taxable income over a number of years is by itself strong evidence of fraud. (Baumgardner v. Commissioner, 251 F.2d 311; Harold S. Lutsko, T.C. Memo., April 17, 1969.) In view of all of these circumstances, Mr. Tuchinsky's explanation that he thought his income levels were too low to create tax liabilities is unconvincing. (Robert G. Tyson, T.C. Memo., Feb. 28, 1950.) We conclude that the deficiencies involved in this case were due to fraud with intent to evade tax.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

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IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Herbert Tuchinsky against proposed assessments of additional personal income tax and penalties in the total amounts of \$522.47 \$76,638 and \$1,346.12 for the years 1959, 1960 and 1961, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 1st day of July, 1970, by the State Board of Equalization.

Robert J. [Signature], Chairman
John W. [Signature], Member
[Signature], Member
[Signature], Member
[Signature], Member

ATTEST: [Signature], Secretary