

Appeal of J. 'Pascal de Filippis

The questions presented by this appeal are whether appellant has demonstrated error in respondent's proposed assessment of, underreported income and whether appellant has demonstrated error in respondent's proposed assessment of a negligence penalty,

During 1978, appellant was employed as a waiter, first by Le Saint Tropez restaurant in Newport Beach, California, and later that year by La Bourgogne, a continental cuisine restaurant in San Francisco, California.

Waiters at La Bourgogne worked in pairs, and each pair split equally the tips they derived from their services. Cash tips were typically collected by the waiters from the individual tables, while the waiters kept running totals of charged tips which they presented to the restaurant's cashier for payment at the end of each shift. La Bourgogne kept no independent records of each waiter's tips: it simply required that each waiter submit a monthly total of tips received. It was each waiter's individual responsibility to keep accounting records detailed enough to ensure these monthly totals were accurate. La Bourgogne determined withholding taxes on the basis of those monthly tip-total reports as well as the hourly wages which the restaurant paid each waiter. Yearly summations of tips reported to the restaurant appeared on each waiter's W-2 forms. Appellant's 1978 W-2 form from La Bourgogne reported income of \$864.65 in salary and \$925.00 in tips.

In 1981, respondent conducted a general examination of La Bourgogne's records to verify the accuracy of the tip incomes reported by its waiters for 1977 and 1978. Daily sales records from 28 days were randomly selected in each year and were examined, and individual receipts with tips recorded were segregated from those with no record of tips. Receipts with tips recorded comprised 87 percent of total La Bourgogne sales. The overall percentage of those tips to those sales was 17.155 percent for 1977 and 16.992 percent for 1978. Those percentages were each reduced by 15 percent to account for the amount of the tips the waiters shared with the busboys and the maitre d's (called payouts). The resulting percentages were then multiplied by the restaurant's total receipts for each respective year, and the products were divided by the total hours all waiters worked in each respective year to reach an estimated average tip income per waiter per hour of \$13.12 in 1977 and \$14.00 in 1978.

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Appellant worked a total of 216 hours at La Bourgogne in 1978. Multiplying appellant's 216 hours by the estimated hourly tip income for 1978 of \$14.00, respondent estimated that appellant's 1978 tip income from La Bourgogne was \$3,024. Respondent applied the ratio of estimated tips received to wages paid by La Bourgogne, \$3,024 to \$864.65 or 3.5 to 1, to the reported wages appellant received at Le Saint Tropez. Respondent estimated that appellant had received \$5,817 in tips while employed at Le Saint Tropez although the 1978 tip income reported for appellant by the Le Saint Tropez W-2 was only \$1,740. Respondent concluded that appellant had significantly underreported his actual income from tips in 1978 and later issued a proposed assessment of additional tax and fraud penalty.

Respondent then held conferences with appellant, as well as with other waiters in similar circumstances. As a result, the 15 percent allowance for busboy and maitre d' hotel payouts was increased to 20 percent and the fraud penalty originally proposed in appellant's assessment was abated and replaced with a negligence penalty. Based upon appellant's statements that Le Saint Tropez was a smaller, less formal restaurant and that the waiters' payouts were larger, respondent reduced its estimated tips to wages ratio for that restaurant to 1.65 to 1, and modified the amount of its assessment against appellant to reflect all those adjustments. Respondent sustained its assessment as so modified. This appeal followed.

The California Personal Income Tax Law requires a taxpayer to state specifically the items and amount of his gross income during the taxable year. Gross income includes all income from whatever source derived unless otherwise provided in the law. (Rev. & Tax. Code, § 17071.) Every taxpayer is required to maintain accounting records that will enable the taxpayer to file an accurate return. (Former Cal. Admin. Code, tit. 18, reg. 17561, subd. (a)(4), repealer filed June 25, 1981 (Register 81, No. 26).)

In the absence of such records, the Franchise Tax Board is authorized to compute income by whatever method will, in its opinion, clearly reflect the income. (Rev. & Tax. Code, § 17561, subd. (b); Breland v. United States, 323 F.2d 492 (5th Cir. 1963); Harold E. Harbin, 40 T.C. 373 (1963); Appeal of John and Codelle Perez, Cal. St. Bd. of Equal., Feb. 16, 1971.) No particular

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method of reconstructing income is required, since the circumstances will vary in individual cases., (Harold E. Harbin, supra.) The existence and amount of unreported income may be demonstrated by any practical method of proof that is available. (See, e.g., Davis v. United States, 226 F.2d 331 (6th Cir. 1955); Agnellino v. Commissioner, 302 F.2d 797 (3rd Cir. 1962); Isaac T. Mitchell, ¶ 68,137 P-H Memo. T.C. (1968), affd., 416 F.2d 101 (7th Cir. 1969); Appeal of John and Codelle Perez, supra; Appeal of Walter L. Johnson, Cal. St. Bd. of Equal., Sept. 17, 1973.)

Where appellant has not supplied detailed records of his income, respondent's determination of a deficiency resulting from its estimate of his income through the use of an approximately accurate formula is presumed correct. (Mendelson v. Commissioner, 305 F.2d 519 (7th Cir. 1962); Meneguzzo v. Commissioner, 43 T.C. 824 (1965); Montie J. Marvin, ¶ 80,509 P-H Memo. T.C. (1980).) The burdens on the taxpayer to prove that the correct income was an amount less than that on which the deficiency assessment was based. (Kenney v. Commissioner, 111 F.2d 374 (5th Cir. 1940); Appeal of John and Codelle Perez, supra.)

On numerous occasions the federal courts have recognized the applicability of these principles in the reconstruction of income from tips, specifically approving a variety of formulary estimates. (Anson v. Commissioner, 328 F.2d 703 (10th Cir. 1964); Mendelson v. Commissioner, supra; Meneguzzo v. Commissioner, supra; Montie J. Marvin, supra.) Respondent's method of estimating appellant's income from tips was generally similar to methods of estimating tip income previously contemplated and approved by federal courts.

Appellant challenged respondent's estimate of his income by stating that his records showed his tip income for 1977 to be the sum of \$399.92, \$384.93, and **\$248.72--\$1,033.57**. He also stated that part of his 1978 La Bourgogne tip income was paid and reported in 1979. Finally, he attacked the ratio used in estimating his tip income from Le Saint Tropez on the ground that respondent's ratio was based on data derived from throughout the whole calendar year, while he was only employed by Le Saint Tropez for five months in that calendar year.

Appellant's statement that his records show total tip income which differs from respondent's estimate is not equivalent to a production of detailed records by

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him. It is simply a general statement that respondent's estimate is incorrect. As such, it is insufficient to sustain his burden of proof that respondent's estimate is incorrect. (Meneguzzo v. Commissioner, supra; Montie J. Marvin, supra.) Appellant's statement that part of 1978 income was reported (by his employers) for 1979 is not convincing in the light of our understanding that each waiter's tips, both cash and charge, were collected by him from the customer and the restaurant during the day in which they were earned. Further, that statement does not actually challenge the correctness of respondent's estimate of his 1978 income. Finally, appellant does not point out why the use of a whole year's data base to estimate his 5-month Le Saint Tropez income would result in an incorrect estimate of his income for that period. In summary, appellant has stated that respondent's estimate was incorrect and implied that its data and methodology were imperfect, but he has not sustained his burden of proof by demonstrating that the amount of the estimate was incorrect and that some other amount was correct.

Finally, as to the negligence penalty imposed by respondent, appellant's failure to produce accurate, detailed records from which his income can be calculated is negligence in itself. (Mendelson v. Commissioner, supra; Meneguzzo v. Commissioner, supra; Montie J. Marvin, supra.)

Accordingly, we have no alternative but to sustain respondent's action.

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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,

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 J. Pascal de Filippis against a proposed assessment of additional personal income tax and penalty in the **total** amount of **\$228.90** for the year **1978**, **be** and the same is hereby sustained.

Done at Sacramento, California, this 10th day of October , 1984, by the State Board of Equalization, with Board Members Mr. Nevins, Mr. Dronenburg, Mr. Collis, Mr. Bennett and Mr. Harvey present.

<u>Richard Nevins</u>	, Chairman
<u>Ernest J. Dronenburg, Jr.</u>	, Member
<u>Conway H. Collis</u>	, Member
<u>William M. Bennett</u>	, Member
<u>Walter Harvey*</u>	, Member

*For Kenneth Cory , per Government Code section 7.9