STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
HYGRADE CASKET CORPORATION	:	DECISION DTA No. 809681
for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period March 1, 1987 through August 31, 1990.	:	

Petitioner Hygrade Casket Corporation, c/o Service Corporation International, Attn: Steve Mack, 1504 Third Avenue, New York, New York 10028, filed an exception to the determination of the Administrative Law Judge issued on March 18, 1993. Petitioner appeared by Snow Becker Krauss P.C. (Harvey Krauss, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Carroll R. Jenkins, Esq., of counsel).

Both petitioner and the Division of Taxation filed briefs. Petitioner filed a reply brief, received on June 17, 1993, which began the six-month period to issue this decision.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUES

I. Whether the Division of Taxation properly determined that the expenses of Hygrade Casket Corporation, which were allocated to its parent corporation, were subject to sales and use taxes on the basis that the allocation constituted additional consideration for the sales of caskets to the parent corporation.

II. If so, whether the amount of the assessment was properly calculated.

III. Whether petitioner has shown that its failure to pay the proper amount of tax within the time required was due to reasonable cause, thereby warranting remission of penalty and reduction of the statutory interest to minimum interest.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "18" which has been modified. The Administrative Law Judge's findings of fact and the modified finding of fact are set forth below.

On May 13, 1992, the parties entered into a written stipulation of facts, the contents of which have been incorporated into the following Findings of Fact, except as otherwise noted.

Pursuant to a field audit of Hygrade Casket Corporation ("Hygrade") which commenced in September 1989, the Division of Taxation ("Division"), on April 26, 1991, issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due to Hygrade in the amount of $76,201.75, plus penalty and interest, for a total amount due of $121,576.69 for the period March 1, 1987 through August 31, 1990.

As will be discussed below, the audit resulted in additional sales and use taxes due from Hygrade, other than the amount asserted in the notice of determination. However, these amounts were agreed to and paid by Hygrade. Therefore, it is only the $76,201.75, plus penalty and interest, which remains at issue herein.

Prior to the issuance of this assessment, certain of Hygrade's officers executed consents extending the period of limitation for assessment of sales and use taxes as follows:

Date Executed	Periods Extended	Date for Assessment
5/16/90	3/1/87 - 8/31/87	12/20/90
12/10/90	3/1/87 - 2/29/88	6/20/91

On April 16, 1990, the auditor (David Gibson) sent an appointment letter to Hygrade in Houston, Texas which advised that an audit would be conducted, at Hygrade's office, on May 7, 1990. The letter requested that all books and records pertaining to Hygrade's sales and use tax liability be made available.

Mr. Gibson testified that the records presented were deemed adequate for the performance of a detailed audit. However, on May 15, 1990, a representative of Hygrade executed an audit method election form whereby it was agreed that a test period audit would be

performed to audit sales and recurring expense purchases; fixed asset acquisitions would be audited in detail.

Hygrade was a wholly-owned subsidiary of Service Corporation International ("SCI"), with a mailing address c/o Service Corporation International, 1504 Third Avenue, New York, New York. SCI was a publicly-owned corporation with offices in Houston, Texas as well as in New York City.

SCI dealt with every aspect of funerals, from caskets to flowers to limousines. It established separate corporations to deal with particular areas of the funeral business.

During the audit period, SCI operated wholly-owned funeral homes throughout the United States, including approximately 35 which were located in the New York City metropolitan area.

Hygrade's sole business purpose during the audit period was to purchase, warehouse and ultimately deliver caskets to SCI's funeral homes in the New York City area. It existed for the administrative convenience of relieving individual SCI funeral homes from the necessity of having to deal directly with independent casket manufacturers. Other than Hygrade's dealings with the SCI funeral homes, Hygrade was not engaged in transactions of a retail nature.[1]

When Hygrade delivered or transferred caskets to an SCI funeral home, the computerized bookkeeping charges therefor, which were attended to and maintained by SCI, were based upon Hygrade's purchase price paid to the manufacturer, plus an amount equal to the applicable State sales tax rate. Hygrade remitted the sales tax to the Division upon the filing of its quarterly sales tax returns.

The caskets delivered by Hygrade to the funeral homes were later sold to the public in connection with other funeral services. Hygrade did not provide its services to non-SCI funeral homes.

SCI determined the quantity and quality of Hygrade's inventory. Such determinations were predicated upon projected (anticipated) needs of SCI's funeral homes in the New York

---

[1]Paragraph "5" of the stipulation of facts sets forth the parties' positions with respect to "retail" transactions. These positions will be set forth in a separate portion of the determination.

metropolitan market.

Hygrade acquired its inventory as completed products and was not engaged in repairing, upgrading, altering or, in any way, enhancing the value of its casket inventory. The prices which Hygrade paid to its casket manufacturers for its inventory were competitive, on an industry-wide basis, with the per casket price at which such manufacturers sold caskets to nonrelated funeral home entities.

SCI allocated Hygrade's out-of-pocket operating costs to SCI's funeral homes at the end of each year, at which time Hygrade's sales and expenses were closed out to zero. Any expense balances remaining at that time were allocated through accounting entries to the SCI funeral homes to which Hygrade provided caskets. The auditor determined that the additional allocation of these year-end expenses to the SCI funeral homes represented an additional sales price for the caskets to the funeral homes. The computation giving rise to this assessment will be hereinafter more fully explained.

The audit report indicates (and the auditor testified at the hearing) that, during the audit, the journals and bookkeeping entries showing the allocations to the SCI funeral homes were initially provided to the auditor, but when he requested to make copies thereof, Hygrade's legal department denied him access to the journals and bookkeeping entries. They were not again made available to the auditor.[2]

Hygrade's acquisition of fixed assets was audited in detail for the entire audit period and an additional tax in the amount of $1,567.36 was assessed. Hygrade's sales tax accrual account was examined in detail and errors (debits that could not properly be accounted for) were found which resulted in additional tax due of $14,889.98. Additional tax due on expense purchases was assessed in the amount of $48,322.43. A refund previously issued in the amount of $12,659.20 was denied on the basis that Hygrade had previously taken credit for it. These amounts were agreed to by Hygrade and were paid in full (see, above).

---

[2]A portion of paragraph "12" of the stipulation relates to the computation of the assessment at issue which will hereinafter be fully set forth. Paragraphs "13" and "14" of the stipulation contain Hygrade's position and a statement of the issue, respectively, and need not be set forth as Findings of Fact.

As previously indicated above, a review of Hygrade's books and records indicated that Hygrade, at the end of each year, was closing out to a zero balance, i.e., its income and expenses were allocated to the various SCI funeral homes. Such allocations appeared on the tax returns of the funeral homes. In addition, Hygrade, the funeral homes and the other SCI funeral entities filed consolidated tax returns. The auditor requested the journals containing the adjusting and closing entries from Hygrade's legal department which were initially provided. However, when the auditor expressed a desire to make copies of these entries, he was told that the journals were confidential and he was denied access to these records. Due to the fact that he was denied access, the auditor estimated tax due on these year-end allocations which he determined constituted an additional price for caskets provided by Hygrade to the funeral homes.

The estimate was based upon two financial statements which were made available to him; one statement was for the year ended December 31, 1989 and the other financial statement was for the nine-month period January 1 through September 30, 1990. Expenses (referred to as intercompany assistance on the financial statements) were $270,929.00 for the year ended December 31, 1989 and $190,603.00 for the nine-month period ended September 30, 1990. Utilizing the financial statements, the auditor determined additional expenses closed out to the funeral homes (he considered these expenses to be part of the sales price of the caskets) in the amount of $923,657.62, with additional tax due thereon (at 8.25%) of $76,201.75.[3]

There were no sales invoices issued on Hygrade's sales of caskets to the SCI funeral homes; a purchase order system containing essentially the same information was used instead.

The expenses of Hygrade which were allocated to the funeral homes consisted of wages and salaries, general operating expenses, utilities and miscellaneous funeral supplies. There was no transfer of funds from the funeral homes to Hygrade on the sale of the caskets; the transactions were reflected solely through accounting entries performed by SCI.

---

[3]The financial statement for the year ended December 31, 1989, indicating expenses of $270,929.00 ($270,929.00 divided by 12 x 3 = $67,732.25), was used for the period March 1, 1987 through February 28, 1989. The financial statement for the nine-month period January 1 through September 30, 1990, showing expenses of $190,603.00 ($190,603.00 divided by 9 x 3 = $63,534.30), was used for the period December 1, 1989 through August 31, 1990. For the period March 1 through November 30, 1989, the figure of $63,732.24 was used for each quarter. There is no indication how this amount was computed.

During the course of the audit, no inquiry was made as to the number of caskets sold to the funeral homes during the audit period or as to the fair market value of the caskets. The auditor also did not inquire whether or not the funeral homes paid Hygrade or SCI for the bookkeeping allocation.

We modify the Administrative Law Judge's finding of fact "18" to read as follows:

> Joan Goff, comptroller of SCI's funeral division, testified that budgets were prepared for each of the funeral homes based upon their projected revenues (number of funerals). Based upon such projected revenues, a portion of Hygrade's expenses were allocated thereto. The allocations were made for budgetary purposes and for determining the financial performance of each funeral home. The projection was based not on actual use (number of caskets purchased), but on projected performance.
>
> Similar bookkeeping allocations were made with respect to SCI's other funeral entities (casket warehouses, centralized embalming facilities, sign company, etc.). Ms. Goff also testified that there were no accounts receivable and accounts payable entries made to the books of petitioner and SCI, respectively, as a result of the year-end adjustment, nor was there any cash transferred between these entities (Tr., p. 37). She further testified that there were no "agreements between SCI [and] Hygrade . . . which would establish in any way a claim of right or obligation with respect to Hygrade's overhead allocation" (Tr., p. 41). Rather, she stated that "just the expenses" were allocated (Tr., p. 41).
>
> Ms. Goff stated that, in 1990, Hygrade ceased operation and, thereafter, SCI funeral homes purchased caskets directly from manufacturers. Prices paid by the funeral homes for the caskets were comparable to what Hygrade had paid.
>
> Because of Hygrade's existence, the individual funeral homes did not need to employ personnel to order, receive and maintain casket inventories.[4]

OPINION

In the determination below, the Administrative Law Judge held that a sales tax liability arose upon petitioner's transfer of caskets to SCI's funeral homes and upheld in full the amount of tax assessed. Specifically, it was held that: 1) petitioner's transfer of the caskets to SCI met the requirement of a taxable transfer that there be a "transfer of possession" (citing Tax Law § 1101[b][5]); and 2) subsequent expense allocations from petitioner to SCI, despite being accomplished through bookkeeping entries, were additional "consideration" received in

[4]The Administrative Law Judge's finding of fact "18" was modified by adding the second sentence to the second paragraph of this finding to more accurately reflect the record.

exchange for the caskets and, therefore, properly subject to tax by the Division (citing Matter of Coyne Ind. Laundry, State Tax Commn., March 18, 1983; Matter of Hubbell Elec., State Tax Commn., February 4, 1983; Matter of Browning-Ferris Indus., State Tax Commn. Advisory Opinion, January 9, 1986 [TSB-A-86(4)S]).

The Administrative Law Judge also rejected petitioner's argument that the assessment should have been based on the fair market value of the caskets transferred, stating that there was no evidence that the consideration upon which the assessment was calculated, together with the initial charge, did not represent the true value of the caskets. The Administrative Law Judge, in response to petitioner's objection that the Division's auditor made no inquiry as to the number of caskets transferred or the fair market value of the caskets, stated that: (i) the Division's assessment is not based on such information since the tax on these transfers had already been paid; and (ii) because petitioner denied the Division access to its records, the Division was within its rights to assess tax based on "such information as may be available" (citing Tax Law § 1138[a][1]).

On exception, in addition to its disagreement with numerous factual findings by the Administrative Law Judge, petitioner asserts that: 1) the assessment lacked a rational basis and, thus, must be annulled (citing Matter of King Crab Rest. v. Chu, 134 AD2d 51, 522 NYS2d 978); 2) it demonstrated by clear and convincing evidence that the proper basis for the assessment was the wholesale fair market value of the caskets purchased by petitioner from its suppliers, under which method taxes were fully paid; 3) it is entitled to a refund on previous tax expenditures because it provided the auditor with all the information he requested; and 4) reasonable cause was demonstrated for its failure to pay the tax assessed.

In response, the Division argues that: 1) the transfer of caskets by petitioner were transfers of possession for a consideration; 2) the prices paid by petitioner to its manufacturers were competitive; and 3) petitioner has failed to meet its burden of showing that some or all of the year-end allocation entries were not subject to sales tax.

We affirm the determination of the Administrative Law Judge.

Tax Law § 1105(a) provides for the imposition of sales tax upon the "receipts[5] from every sale of tangible personal property . . ." other than certain exceptions not relevant here. Tax Law § 1101(b)(5) defines "sale" as:

> "[a]ny transfer of title or possession or both, exchange or barter, rental, lease or license to use or consume, . . . conditional or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement therefor . . ." (emphasis added).

The amount of sales tax imposed on transfers between related corporations based on "consideration paid" is conditional, as stated in the Division's regulations:

> "[t]he sale of property by one related corporation to another related corporation is a retail sale, and taxable to the extent of the consideration paid, or the fair market value, if the consideration paid is not an adequate indication of the true value of the property transferred" (20 NYCRR 526.6[d][8][i], emphasis added).

It is not disputed that upon the physical transfer of the caskets from petitioner to the SCI funeral homes, there was a "transfer . . . of possession," with at least part of the "consideration" created from bookkeeping entries made by the respective corporations at the time of the transfer.[6] Therefore, in determining the correctness of the assessment, we must decide 1) whether the year-end bookkeeping entries represent additional "consideration" for these property transfers (Tax Law § 1101[b][5]); and 2) if so, whether the total consideration is an adequate indication of the property's fair market value (20 NYCRR 526.6[d][8][i]). In order to invalidate the assessment, petitioner has the burden to prove that the assessment is incorrect (Tax Law § 1132[c]).

---

[5]"Receipt" is defined under the regulations as the:

> "amount of the sale price of any property and the charge for any service taxable under articles 28 and 29 of the Tax Law, valued in money, whether received in money or otherwise" (20 NYCRR 526.5[a]).

[6]Sales tax was remitted by petitioner calculated on the price charged for the caskets as stated in these initial entries.

A partial definition of consideration contained in the regulations[7] fails to explicitly address the facts of this case. This regulation does not attempt to put forth an all-inclusive definition of "consideration," but only sets forth items that are included as consideration. "Consideration" has been more generally defined in the common law as "some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss, or responsibility, given, suffered, or undertaken by the other" (Richman v. Brookhaven Servicing Corp., 80 Misc 2d 563, 363 NYS2d 731, citing Becker v. Colonial Life Ins. Co., 153 AD 382, 138 NYS 491; 21 NY Jur2d § 64, emphasis added). The auditor's notes from the audit stated that at year-end, petitioner's sales and expenses were closed out to zero, with these balances being transferred to SCI's funeral homes. The report further stated that allocating these expenses, in effect, increased the price paid for the caskets by SCI. Therefore, these entries were viewed as an increase in selling price of the caskets and the journal entries to reflect these changes requested from petitioner's legal department were initially provided, but were taken back when photocopies were requested of the entries (Division's exhibit "C," p. 4).

In deciding whether the year-end accounting entries constitute "consideration" within the meaning of section 1101(b)(5), we acknowledge the analytical difficulties inherent in using the term "consideration" in the context of transactions between a parent corporation and its wholly owned subsidiary. The transfer of value (i.e., the shifting of assets and/or the creation of liabilities), which is often the consideration in a contract, is difficult to discern under this scenario because, in substance, the value that is "transferred" merely passes from one pocket of the parent to the other. Thus, we acknowledge that the classification of such transfers as "consideration" or "detriments" in this context is purely formalistic when viewing the corporations as a single economic unit, but one that is required under the statute, the regulations

---

[7]The term "consideration" is partially defined under the regulations as follows:

> "consideration includes monetary consideration, exchange, barter, the rendering of any service, or any agreement therefor. 'Monetary consideration' includes assumption of liabilities, fees, rentals, royalties or any other charge that a purchaser, lessee or licensee is required to pay" (20 NYCRR 526.7[b], emphasis added).

and the case law in applying the sales tax (see, Matter of 107 Delaware Assocs. v. New York State Tax Commn., 64 NY2d 935, 488 NYS2d 634; Matter of Motion Marketing Assocs., Tax Appeals Tribunal, July 23, 1992; Matter of Tops, Inc., Tax Appeals Tribunal, November 22, 1989).[8]

It is undisputed that "accounting entries" were made to the consolidated books of these corporations at the end of the years at issue. Because petitioner refused to allow a thorough examination of these entries at the time of the audit, it is now faced with the burden of establishing that the entries did not constitute additional consideration given by SCI in exchange for the caskets it received from petitioner. We find that petitioner has not met this burden. At hearing, petitioner, through the testimony of Ms. Goff, stated that the entries did not: (i) increase SCI's accounts payable account or otherwise create an obligation on the books of SCI; (ii) increase petitioner's accounts receivable account or otherwise create a claim of right with respect to petitioner or (iii) represent a cash payment by SCI to petitioner. However, petitioner has not eliminated the possibility that the year-end entries could have reduced an intercompany asset account of SCI, which could be classified as "consideration" under this analysis. For instance, when one corporation (parent) owns another corporation (subsidiary), this ownership is accounted for on the parent's books in an asset account titled "Investment in Subsidiary" (Pahler and Mori, Advanced Accounting Concepts and Practice at 60 [3rd ed.]). Thus, where expenses are shifted from the subsidiary to the parent through a debit entry to the parent's expense account, it is possible that an offsetting credit entry was made to the parent's "Investment in Subsidiary" account.[9] The reduction in this asset account, a scenario not addressed by the testimony of Ms. Goff, would constitute "consideration" under this analysis.

---

[8]Indeed, the regulations acknowledge the potential of this formalistic approach to diverge from economic reality by providing an alternate valuation basis for imposing sales tax - fair market value - if the "consideration" transferred is not indicative of the "true value of the transferred property" (see, 20 NYCRR 526.6[d][8][i]).

[9]We acknowledge that the "expenses" transferred from petitioner may have been of a nature that would have ordinarily required them to be capitalized on SCI's books by debiting SCI's inventory account (see, 26 USC § 263A; 2 Merten's, Federal Income Taxation § 16.31 et seq). However, this would have no impact on valuing the consideration paid by SCI, as the corresponding credit entry would still have been a reduction to an asset account of SCI, constituting a detriment to SCI.

This possibility coupled with the fact that petitioner did not introduce the accounting records of the corporations to confirm Ms. Goff's testimony leads us to conclude that petitioner has not established that year-end entries did not constitute "consideration" given by SCI for the transferred assets.

Despite our conclusion above, petitioner has the opportunity to prove the assessment incorrect by showing that "the consideration paid is not an adequate indication of the true value of the property transferred" (20 NYCRR 526.6[d][8][i]). However, petitioner has failed to present any documentation as to the "true value" of the caskets received by SCI during the years at issue. Therefore, petitioner has not shown that this conditional fair market value method would have been used in this case.

We next address petitioner's contention that the calculation of the assessment was without a rational basis and, therefore, the assessment should be annulled as a matter of law. Petitioner contends that the auditor's failure to request from petitioner information pertaining to the number of caskets transferred to SCI during the period at issue and the fair market value of the caskets, the assessment is erroneous as a matter of law, and must be annulled (Petitioner's brief, pp. 9-10).

In analyzing this issue, it is important to recognize the conditional standard for imposing tax on sales between related corporations. Under this standard, sales are taxable in the first instance "to the extent of the consideration paid . . ." (20 NYCRR 526.6[d][8][i]). Because petitioner (who carries the burden to prove the assessment incorrect) has failed to establish that the year-end entries were not consideration, these estimated amounts were included in the taxable base. The regulation further states that this "consideration" standard will not be used only "if the consideration paid does not indicate the true value of the property transferred" (20 NYCRR 526.6[d][8][i]). Therefore, the question is whether the Division's use of the primary "consideration paid" valuation method has been shown to be without a rational basis in this instance.

We have addressed the rational basis requirement of an assessment in Matter of Atlantic

& Hudson Ltd. Partnership (Tax Appeals Tribunal, January 30, 1992), where we stated:

> "[a]lthough a determination of tax must have a rational basis in order to be sustained upon review (see, Matter of Grecian Sq. v. New York State Tax Commn., 119 AD2d 948, 501 NYS2d 219), the presumption of correctness raised by the issuance of the assessment, in itself, provides the rational basis, so long as no evidence is introduced challenging the assessment (see, Matter of Tavolacci v. State Tax Commn., 77 AD2d 759, 431 NYS2d 174; Matter of Leogrande, Tax Appeals Tribunal, July 18, 1991)."

In the Atlantic & Hudson case, we also reaffirmed the principle that "the Division does not have the burden to demonstrate the propriety of the assessment and that the petitioner has a heavy burden to prove the assessment erroneous" (citing Matter of A & J Gifts Shop v. Chu, 145 AD2d 877, 536 NYS2d 209, lv denied 74 NY2d 603, 542 NYS2d 518; Executive Land Corp. v. Chu, 150 AD2d 7, 545 NYS2d 354, appeal dismissed 75 NY2d 946, 555 NYS2d 692; Matter of Blodnick v. New York State Tax Commn., 124 AD2d 437, 507 NYS2d 536; Matter of Scarpulla v. State Tax Commn., 120 AD2d 842, 502 NYS2d 113).

Because petitioner failed to present any evidence tending to establish the inaccuracy of the valuation method used by the Division (specifically, evidence of the number of caskets sold during the period at issue and their respective fair market values), we hold that petitioner has failed to prove that the primary valuation method for assessing sales tax under the regulation was irrational (Matter of Atlantic & Hudson Ltd. Partnership, supra; 20 NYCRR 526.6[d][8][i]).

In support of this argument that the assessment lacked a rational basis, petitioner cites Matter of Adamides v. Chu (134 AD2d 776, 521 NYS2d 826, lv denied 71 NY2d 806, 530 NYS2d 109) for the proposition that the Division has a duty "to request information relevant to the taxes at issue, and to base [its] determination on that information if . . . available" (Petitioner's brief, p. 10). In support of this argument, petitioner established, during cross-examination of the Division's auditor, that the auditor never requested information pertaining to the number of caskets sold by petitioner or their respective "true values" (Tr., p. 27).

In stating this position, petitioner would appear to argue that in absence of the year-end adjusting entries (whose absence was a direct result of petitioner's failure to provide them), the

Division was then compelled to further request fair market values from petitioner. We disagree. In our opinion, at the time petitioner refused to provide the year-end accounting entries, the Division was authorized to estimate the tax liability on the basis of external indices (Tax Law § 1138[a][1]; Matter of Ristorante Puglia, Ltd. v. Chu, 102 AD2d 348, 478 NYS2d 91, 93). In order for petitioner to show that the method employed by the Division (an estimation of "consideration paid") was not an "adequate indication" of the aggregate "true value" of these intercorporate sales, it was petitioner who was required to present evidence establishing this fact (see, Matter of Atlantic & Hudson Limited Partnership, supra; 20 NYCRR 526.6[d][8][i]). In the absence of such proof, the method employed by the Division must stand. To hold otherwise would encourage taxpayers to withhold records on audit both to make the auditor's task more difficult and to create a basis to attack the audit results.

Finally, we address petitioner's arguments that: (i) it is entitled to a refund on previous tax expenditures because it provided the auditor with all the information he requested and (ii) reasonable cause was demonstrated for petitioner's failure to pay the tax assessed. Because we find that the Administrative Law Judge correctly and adequately addressed these issues, we affirm based on the determination of the Administrative Law Judge.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Hygrade Casket Corporation is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Hygrade Casket Corporation is denied; and

4. The Notice of Determination dated April 26, 1991 is sustained.

DATED: Troy, New York
December 16, 1993

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner