STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
KENNETH SCHUCK TRUCKING, INC.	:	DECISION DTA NO. 816129
for Revision of a Determination or for Refund of Highway Use Tax under Article 21 of the Tax Law for the Period April 1, 1990 through June 30, 1995.[1]	:	

Petitioner Kenneth Schuck Trucking, Inc., 1030 Blue Barn Road, Allentown, Pennsylvania 18104, filed an exception to the determination of the Administrative Law Judge issued on January 13, 2000. Petitioner appeared by Joseph T. Bambrick, Jr. & Associates, P.C. (Joseph T. Bambrick, Jr., Esq.). The Division of Taxation appeared by Barbara G. Billet, Esq. (John E. Matthews, Esq., of counsel).

Petitioner filed a brief in support of its exception. The Division of Taxation did not file a brief in opposition. Oral argument, at petitioner's request, was heard on September 14, 2000 in New York, New York.

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

[1]Post-hearing it was determined by the Division of Taxation that petitioner was not advised of an extension of the audit period beyond June 30, 1994, nor were records requested for such extended period. Pursuant to ***Matter of Adamides v. Chu*** (134 AD2d 776, 521 NYS2d 826, ***lv denied*** 71 NY2d 806, 530 NYS2d 109), the tax assessed by the Division of Taxation based upon an asserted lack of books and records, for the four quarters between July 1, 1994 and June 30, 1995, was canceled.

ISSUES

I. Whether the Division of Taxation conducted a proper test period audit of petitioner's business operations.

II. Whether an assessment of truck mileage tax and fuel use tax is a violation of the Commerce Clause of the United States Constitution.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "5," "6," "7," "11" and "26" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

The Division of Taxation ("Division") issued two notices of determination to petitioner, Kenneth Schuck Trucking, Inc., ("Schuck"), dated January 29, 1996. The first is an assessment of highway use tax, specifically truck mileage tax ("TMT"), in the amount of $263,906.57, plus interest and penalty in the amounts of $60,297.46 and $71,093.46, respectively, totaling $395,297.49, for the period April 1, 1990 through June 30, 1995. The original amount of TMT assessed ($263,906.00) has two components: $187,646.00 computed from the self-assessment of mileage reported on petitioner's tax returns for fuel use purposes, where no amount was paid for TMT on such miles; and secondly, $76,260.00 for additional miles based upon the test period audit conducted. The latter amount was reduced by recorded mileage adjustments and other corrections amounting to $6,674.00 during the hearing, and $15,058.00 for tax assessed after June 30, 1994, since the Division determined petitioner had not received proper notification of the audit period beyond that point (***see,*** Footnote 1), for the resulting field audit portion of

$54,528.00. The amount of TMT thus in issue for purposes of this determination is $242,174.00, plus penalty and interest.

The second notice assessed highway use tax, specifically fuel use tax ("FUT"), in the amount of $93,019.35, plus interest and penalty in the amount of $21,967.44 and $25,310.47, respectively, for the period April 1, 1990 to June 30, 1995. The FUT assessed has two components: $72,993.00 in FUT assessed for the additional miles resulting from the test period audit, and $20,026.00 in FUT from mileage per gallon ("MPG") adjustments (described *infra*). Collectively ($93,019.00), these amounts were reduced by two items: recorded mileage and other adjustments in petitioner's favor in the amount of $5,785.00, and $23,578.00 for tax assessed after June 30, 1994, since the Division determined petitioner had not received proper notification of the audit period beyond that point (***see,*** Footnote 1). This resulted in FUT in issue in the amount of $63,656.00 (represented by $49,970.00 from the assessment of additional miles and $13,686.00 from MPG adjustments), plus penalty and interest.

Several consents extending the statute of limitations were executed during the audit, with the latest being executed on August 9, 1995, extending the time during which TMT and FUT could be assessed until March 31, 1996, for the period April 1, 1990 through March 31, 1994.[2]

Petitioner, a Pennsylvania corporation located in Allentown, Pennsylvania, was a motor carrier with operating authority from the Interstate Commerce Commission during the periods in

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[2] Although the two notices of determination issued in this matter were within the time frame set forth by the consent extending the statute of limitations, the period for which tax was to be assessed was misstated as ending March 31, 1994, rather than June 30, 1994, as defined by the Division's appointment letter. The assessment for the period April 1, 1994 to June 30, 1994 will not be rendered invalid, however, since the statute of limitations is an affirmative defense which is deemed waived if not raised. In this case, neither party raised the mistake as an issue, and have continued to contest the assessment as though it extended to June 30, 1994 (***see***, ***Matter of Richards***, Tax Appeals Tribunal, December 3, 1991).

issue. As pertinent to this matter, petitioner transported shipments to and from points in New York State primarily from its facilities in Allentown.

The notices sent to petitioner were issued as a result of an audit of petitioner's operations for the period in question, which was commenced in August 1994. Initially the auditors assigned to this matter were Robert Stewart and Dennis Williams, with the former being the principal auditor until he became ill, and subsequently retired. Mr. Stewart did not testify at the hearing.

The audit was commenced by the mailing of an appointment letter dated August 10, 1994, from Mr. Stewart to petitioner. The correspondence described the nature of the field audit which the Division was to conduct, i.e., a field audit of petitioner's New York State truck mileage and fuel use taxes (in addition to corporation franchise taxes, which are not the subject of this determination). The letter explained:

> Our audits are usually performed on a test period basis. Normally, the test period selected is a month or quarter within the last twelve months of the audit period. Although test period audits are usually conducted to facilitate the audit process, all books, records, worksheets, and other documents pertinent to the preparation of your tax returns, as well as all information requested on the attached sheet, are to be made available for the entire audit period.

The attached sheet indicated that the following books and records pertinent to the TMT and FUT examination should be available at the commencement of the audit:

> Truck Mileage and Fuel Use Taxes
> Tax Returns (MT-903's)
> Mileage records (I.C.C. logs, odometer readings, trip sheets)
> Fueling records (bulk fuelings, retail fuel receipts)
> Thruway receipts and statements

We modify finding of fact "5" of the Administrative Law Judge's determination to read as follows:

> Petitioner's records were substantially available for the audit period, with the exception of some Interstate Commerce Commission ("ICC") logs, required by Federal regulations to be retained for a period of six months, and generally used to record mileage and other details about the trips taken by the truckers. Petitioner complied with the Federal requirement that logs be maintained for six months, but did not retain logs prior to that time. Although trip sheets, also called daily trip reports ("DTRs") were provided to the Division, in most cases there is additional detail contained in the logs which is not duplicated in the DTRs, such as intermediate destination points, which is useful in the context of an audit of TMT and FUT where trips are replicated. The Federal mandated logs for the test period which later became the subject of this audit, were available for the Division's review.[3]

We modify finding of fact "6" of the Administrative Law Judge's determination to read as follows:

> In the early stage of the audit, which took approximately one week of field audit work, Mr. Williams testified that Mr. Stewart made the decision that petitioner did not maintain complete records for the entire audit period, but it is unclear from the record what records, if any, Mr. Stewart reviewed prior to reaching this conclusion (Hearing Tr., pp. 49-51). Neither the audit report nor Mr. Williams' testimony shows the process followed, or the records that were reviewed by the auditors, prior to reaching the conclusion that the books and records were inadequate for the audit period. The auditors' contact sheets reflect that a decision had already been made to conduct a test period audit before the auditors reached the audit location (***see***, Exhibit "G"). Further, Mr. Williams testified that there was really no need for a complete set of books and records for the four year audit period, because they (the auditors) already knew they would be conducting a test period audit. "So normally we just see records for the audit period, the

[3]We modified finding of fact "5" of the Administrative Law Judge's determination to more accurately reflect the record.

> test period itself, but I believe that the other records were pretty much available" (Hearing Tr., p. 49).
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> When the Administrative Law Judge asked Mr. Williams specifically what documents were reviewed prior to determining that the taxpayer's books and records were inadequate, Mr. Williams' answer was unresponsive. He merely stated again that the logs were only available for a six month period (***see***, Hearing Tr., p. 291). Mr. Williams also testified that the ICC logs were not always important to the audit, because they did not provide information that could not be obtained in other documents (***see***, Hearing Tr., p. 289, 291).
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> Once it was determined that the taxpayer's books and records were inadequate for the whole audit period, it was deemed unnecessary to request that the taxpayer sign an Audit Method Election Agreement.[4]

We modify finding of fact "7" of the Administrative Law Judge's determination to read as follows:

> In conducting this audit, the Division chose a test period which the auditors felt was representative and was within six months of the commencement of the audit when the driver's logs were more likely to be available. In this case, the test period April 1, 1994 through June 30, 1994 was chosen because all the records were available. Mr. Williams was not aware of any additional reason that was used by Mr. Stewart in choosing the second quarter of 1994, whether such choice had any assurance of being a random selection, or whether it, in fact, represented a typical period. When a test period audit is performed, the Division concentrates on the test period. Accordingly, the auditors did not check actual trips for any period outside the test period. No error rate was calculated for other quarters in the audit period to determine whether the quarter chosen bore a similar error rate.[5]

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[4]We modified finding of fact "6" of the Administrative Law Judge's determination to more accurately reflect the record.

[5]We modified finding of fact "7" of the Administrative Law Judge's determination to more accurately reflect the record.

During the test period the Division does not audit all the units that operated during that time frame. Regarding the selection of unit trucks within the test period, the Division's auditor established that the trucks are chosen randomly, for example, every third or fifth unit is examined from a list provided a taxpayer. In general, there are no specific criteria, special standards or predetermined selection samples used in making the random selection. In this case, Mr. Stewart chose the random sample and Mr. Williams was not privy to the factors used by Mr. Stewart in making the random selection. The instructions provided Mr. Williams were to begin at one end of the list and Mr. Stewart would begin at the other, until the random selection led them to the middle of the list. In all, eight units were chosen to be audited.

In addition to owning its own vehicles, petitioner also had a relationship with two other trucking operations. Happiness Trucking, also owned by Mr. Schuck, operated its own vehicles which, for part of the audit period, were leased to petitioner. T&A Enterprises was a separate company with owners which did not include Kenneth Schuck. In the case of T&A, owner-operators leased their trucks to petitioner or carried loads for Mr. Schuck under a lease agreement. A sample lease agreement was contained in the audit file; however, Mr. Williams was not entirely familiar with its provisions.

Although Mr. Williams could not identify the number of vehicles that petitioner operated during any one quarter during the audit period, he was informed by petitioner that there were approximately 110 vehicles regularly at petitioner's place of business throughout the audit period. Notes contained in the audit file indicated that petitioner had 55 company-owned units and 50 to 60 owner-operators. If an owner-operator purchases his own highway use permit from New York State, he may also be reporting miles for TMT and FUT purposes on his own

company's returns. However, an owner-operator may also report such miles under the name of the company to whom he leased his truck, i.e., petitioner. In the early stages of the audit, there was no attempt by the Division to determine how the owner-operators handled the reporting of miles or which owners had their own permits. However, at some point later in the audit, admitting the importance of this information, the Division determined that some drivers had their own permits and others did not. Some time after the Division had completed its field audit work, the Division identified some of the owner-operators and further reviewed their records.

With respect to the entities Happiness and T&A, the Division could tie the miles driven into the returns filed. However, as to the trips run by owner-operators, the Division was unable to independently verify that the miles driven by the owner-operators were, in fact, reported on petitioner's returns.

We modify finding of fact "11" of the Administrative Law Judge's determination to read as follows:

> During the audit, the Division would inform petitioner if additional records were needed to support petitioner's position for the test period. For example, when petitioner indicated that additional substantiation was available, petitioner was asked, at conferences held between the parties, to provide such documentation, i.e., additional Thruway receipts for trips. When the Division believed such documentation supported adjustments in petitioner's favor, such were made. On the other hand, when petitioner proffered six file drawers of books and records for review, the auditor refused because it was not deemed "new information" (Hearing Tr., pp. 216-218).[6] Mr. Williams was asked how he knew what data was in the files if he did not look at it, to which he replied, "We were told probably what they are

[6]The testimony is unclear as to whether these six file drawers contained data for the whole audit period or merely for the test period.

> basically and the records that we had already reviewed before" (Hearing Tr., p. 216). It is unclear who "told" them.[7]

After the selection of the test period, the auditor randomly selected a unit (a particular truck cab) and using the corresponding driver logs, trip sheets, Thruway receipts, fuel receipts, and computer report, duplicated the trip. The sample of units to be tested was provided to Mr. Williams by Mr. Stewart. Mr. Williams was not provided any guidance as to the number of vehicles that should be audited based on the size of the fleet, and did not refer to any information to define a valid random sample for the test period. The Division did not determine an error factor in the selection of the random fleet. Mr. Williams merely defined a "random sample" as one in which there is no systematic manner of being chosen, and was unaware whether a method was employed in the audit to insure randomness.

Mr. Williams performed the mapping of the trips and prepared Trip Summary 1 ("TS1"). In doing so, Mr. Williams used the Rand McNally Mile Maker computer software package ("Mile Maker") to compute the miles. The Division commonly uses software similar to Mile Maker to estimate mileage if proper records have not been maintained by a taxpayer. Using a AAA New York State map and Mile Maker, Mr. Williams verified the recording of the mileage of five units which were involved in transport during the test period. The mileage of the units examined pursuant to petitioner's mileage and fuel usage report for the test period was compared to the mileage of the units as computed by the auditor. The difference of the two amounts, divided by the miles reported by petitioner is referred to as the error rate, and in this case, was originally determined to be 38.41%. This error rate was then used to project additional miles for

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[7]We modified finding of fact "11" of the Administrative Law Judge's determination to more accurately reflect the record.

TMT and FUT for the audit period. The Division did not assign any type of variance factor to the error rate. Pursuant to discussions between petitioner and the Division, and in accordance with documentation provided by petitioner, adjustments to the TMT and FUT assessed eventually resulted in an error rate of 35.18%.

Mr. Stewart prepared Trip Summary 2 ("TS2"), concerning the mileage of three units, which set forth the origin of a trip, its destinations, toll receipts, and reported miles per the summary. In preparation of TS2, information obtained from petitioner's records was input directly into a computer, and no backup documentation was maintained in the audit file. Mr. Williams continued the audit work performed by Mr. Stewart, and did not review the work Mr. Stewart had already performed. However, Mr. Williams was fully aware that Mr. Stewart prepared TS2 from the same type of documents used by Mr. Williams, even though he did not witness the preparation of each and every segment of the report.

A total of 8 units of 110 were initially examined in the two trip summaries prepared by the Division.[8] For six of these units, the Division could trace the mileage from petitioner's trip sheet to the computer summary used to prepare filed returns. In TS2, for unit #2600, the trip sheets showed 3,436 miles as summarized by the Division's auditor, compared to petitioner's computer record of 6,707. Likewise, also in TS2, for unit #578, the trip sheets resulted in 2,325 miles for the test period, compared to 3,564 miles on petitioner's computer summary. To petitioner's advantage, the Division used the lesser figures in its tax computation.

[8] It was disclosed during the hearing that two vehicles were ultimately deleted from the test period audit. Such trucks were leased to petitioner and driven by George Kester and Elmer Kennedy as owner-operators.

There is no particular State authority for determining miles in an audit of this type. Neither the AAA map nor the Mile Maker are official State approved means for measuring mileage, but in Mr. Williams' experience, they are commonly referred to in audits of this type. In this case, these sources, in addition to petitioner's records, were referenced to compute mileage.

Concerning the calculations of the Mile Maker program, the Division was uncertain whether trailer height restrictions are programmed into Mile Maker so as to effect routing, and possibly the ultimate calculation of miles.

During the audit, it is not common for the auditor to question drivers, and likewise, Mr. Williams did not do so in this case. If the information the auditor obtains from the taxpayer is absent significant detail, the auditor will use a source such as Mile Maker, and not generally contact a driver to ascertain the route of a particular trip. He generally does not check another period for a similar trip, or check another truck driven in the same period. However, if a toll receipt is presented as part of a taxpayer's records, the auditor would attempt to force the trip through the tunnel or over the road represented by the toll receipt. Although each toll receipt is not photocopied so as to become a part of the auditor's file, the auditor takes the information from the receipt and incorporates it into his findings pertinent to the route taken.

James Hamersly, an employee of petitioner who provided testimony at the hearing, established that he was clearly able to drive petitioner's tractor trailers through New York City tunnels, and regularly went to Long Island City through the Holland Tunnel. This was contrary to the route used by Mr. Williams to calculate the mileage using the Mile Maker program which does not generally route through tunnels.

Mr. Hamersly also provided an explanation of the trucking documentation and described how a truck driver was compensated for his runs. Ultimately, as a result of the testimony presented by Mr. Hamersly, the Division agreed to reduce the overall additional mileage it had estimated, and the resulting additional taxes.

The Division was unable to identify any published guideline, State statute or regulation that describes the criteria for choosing a typical audit period or sample from such period. Although petitioner claims there were 60 owner-operators, the Division was aware of approximately 26 from a list prepared during the audit. The Division chose to spot check the records and reviewed the records of eight owner-operators, to determine if they paid TMT. There was no statistical reason provided as to why the TMT of only eight drivers was verified.

Concerning the sample of vehicles, the auditor could not verify that 8 units out of approximately 110 vehicles or the number of audited miles represented a valid sample, or when a sample might be deemed too large. There was no attempt to verify whether the sample was representative of a fleet which made some long trips and some short trips. The Division did not verify whether the runs went from petitioner's New Jersey terminal to points in New York. The Division was unaware of what percentage of the trucks based in Allentown traveled into upstate New York, and what percentage traveled into New York City. Mr. Williams does not believe that the sample chosen for the quarter was necessarily representative of the entire fleet for that quarter, and he does not believe the error rate, as originally calculated was 100% accurate. There was no additional testing of such accuracy and no additional error rates were calculated.

Dr. Craig Moore, an economistician, whose academic strengths are in the fields of economics and statistics, provided expert testimony concerning random samples, and their

significance, in support of petitioner's position. He established that underlying the theory of sampling accuracy is randomness, i.e., that each unit in the population about which estimates are being made must have an equal chance of being selected. He established that the method chosen by the Division to audit the vehicles was not a random sample, but rather represented a systematic sample which, by definition, means a sample where the population does not have an equal chance of being selected. Dr. Moore concluded that the sample of vehicles used was not a reasonably accurate sample, and that the error factor, if calculated, would be so large as to render the estimate unreliable.

In addition, Dr. Moore determined that the selection method (the test period) used for the audit was unreliable and not a professionally acceptable practice. He claims that in order to choose one quarter and draw an inference from that quarter and apply it to 19 or 20 additional quarters, the latter would have to be very similar to the chosen quarter. He stated that a person cannot go back in time three years or project into the future without creating a statistical problem. If a person is not using data that is associated with the time period for which a projection is being made, forecasting into a future area without data runs a high risk of invalidity. He concluded by stating that, in this case, data existed over the 20 quarters of the audit period, and if there had been an adequate sample of that data, done in a proper way and with an appropriate sample size, the Division could have drawn an accurate inference. However, that is not what was done in this case.

Although the Division was aware of Dr. Moore's testimony, and did not believe it to be incorrect, the Division was not inclined to make any changes to the audit on the basis of such

testimony, and maintained that the test period audit was adequate to properly project the liability of other quarters.

TMT payment information pertaining to the quarters in issue, for which petitioner was given credit, was acquired by the Division from the Highway Use Tax Returns (Forms MT-903) for each of the three entities: petitioner, Happiness and T&A. FUT mileage information and FUT payment information were also acquired by the Division from the Highway Use Tax Returns (Forms MT-903) for each of the three entities: petitioner, Happiness and T&A.

Although some owner-operators had filed returns, initially petitioner was given no credit for such taxes because it was unclear whether the Division was assessing for trips that had also been reported by the owner-operators. During the hearing, two owner-operators (Mr. Kester and Mr. Kennedy) provided testimony which resulted in positive adjustments for petitioner. Although the Division did not initiate an attempt to reconcile all owner-operator returns with trips reported by petitioner, petitioner was given credit where any duplication could be shown.

In computing the TMT due, the Division started with petitioner's tax returns for the quarters in issue. Pursuant to Mr. Williams' testimony, mileage information for the 4th quarter of 1990 was unavailable, so an interpolation of the four quarters on either side of that quarter was done to estimate the mileage for that quarter. The Division did not attempt to determine if petitioner was traveling more or fewer miles in New York State for such quarters.

Petitioner's mileage and fuel usage report for the test period, which the Division reviewed for the recording of petitioner's truck mileage, showed MPG (miles per gallon) at 5.66 for each truck. It is unclear why this internal report had the same mileage listed for each vehicle. However, when petitioner filed its returns, it showed MPG calculated out to two decimal places,

ranging from 3.62 MPG to 7.59 MPG. Archer Knight, an employee and truck driver for petitioner established that in 1994 his truck, new to him April 1, 1994, obtained between 6.6 and 6.8 MPG, higher than his previous vehicle, which was estimated at 5.4 to 5.5 MPG. He cited better fuel efficiency in the newer vehicle.

One portion of the FUT assessment is based upon an adjustment concerning miles per gallon. On its FUT returns, petitioner reported MPG factors over the audit period that ranged from 3.62 to 7.59 MPG, based on its business records. During the audit, for any factor over 5.00 MPG, the auditor reduced it to 5.00 and asserted additional FUT for the period, without any apparent consultation with petitioner. For any MPG factor under 5.00, the Division accepted petitioner's records. The reason provided by the Division for the adjustment of MPG's over 5.00, was that such MPG's were large variances over petitioner's normal MPG's, and the adjustment was intended to cure such lack of consistency. In making such adjustment, no consideration was given to current engine manufacturers' information on MPG, the model, make or year of the trucks comprising petitioner's fleet for any portion of the audit period, and whether the recorded mileage was within a predicted range suggested by the manufacturer as appropriate to that vehicle. The Division did not discern whether there was a difference between the T&A fleet and petitioner's fleet, and whether the composition of any of these fleets had changed during the audit period, or between certain quarters. Mr. Williams did not consider the effect of truck load weight differentials on MPG, or that weather conditions and the time of year could have an effect on the MPG. The auditor did not place any significance upon, or question the fact that from the first quarter to the second quarter during each of the years 1992, 1993 and 1994, there was a significant increase in the overall miles recorded by petitioner (between 67,000 and

127,000 additional miles). Although agreeing that certain of the MPG's over 5.00 were reasonable, Mr. Williams still believed that only 5.00 MPG should be allowed.

Rita Tatasciore, petitioner's bookkeeper, provided testimony on petitioner's behalf concerning how information is transmitted from the truck drivers to form the basis for reporting purposes. When a driver returned from a trip, he gave the paperwork for the trip to an employee named Bonnie in petitioner's office. Such paperwork included the driver's delivery receipt, his logs, any mileage reports, and any fuel, toll or other receipts he accumulated during the trip. Bonnie entered the information into the computer for the driver's payroll and for billing purposes, then forwarded the documents to Karen Reeve who checked the logs, and made any corrections before returning them to the drivers. Additionally, Ms. Reeve took the information provided by the drivers and entered the mileage amounts into the computer on the basis of the route traveled and the milage recorded in each state. The drivers based their milage on the direction and route traveled to get to their assigned destination. In the event a driver was on the road for an extended period or not able to drop off his paperwork in the office, petitioner would hold open the reporting for a particular month until approximately the 15th day of the following month in order to associate the milage recorded by the drivers with the month in which the work was performed, even though sometimes the miles were included in a subsequent period. The gallons of fuel purchased were entered into the computer from fuel purchase receipts.

Petitioner's mileage and fuel usage report, a computerized compilation of driver data, for the period April 1, 1994 to June 30, 1994 showed 1,552.83 gallons of fuel purchased in New York. Petitioner's filed form MT-903, combined Truck Mileage and Fuel Use Tax Return shows 717 gallons for the same quarter. Ms. Tatasciore was unable to provide an explanation as to why

there was a discrepancy in the reported difference. However, petitioner believes it is entitled to a credit for such difference.

We modify finding of fact "26" of the Administrative Law Judge's determination to read as follows:

> Petitioner and the Division met to discuss this case and review documents on three occasions: May 16, 1995, June 20, 1995 and August 9, 1995. As noted earlier, additional file boxes of petitioner's records were presented; however, the auditor did not review them, stating that he was "probably" informed that the content was substantially the same as records previously shown to the auditors (Hearing Tr., p. 216).
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> Throughout the hearing, there was a contradiction in the testimony concerning whether the Division was willing to revise audit amounts as petitioner supported its position with documents and explanations. Ms. Tatasciore indicated that, on several occasions during the audit, she met with John Butkins (Mr. Williams' supervisor) and Mr. Williams in their Syracuse office to offer petitioner's paperwork for their review. Although he reviewed a few envelopes of petitioner's paperwork, Mr. Butkins was unwilling to go through the six file boxes of petitioner's documentation, even though Ms. Tatasciore offered to stay several days to tend to the audit. The boxes were delivered to the Division by petitioner in response to the Division's request for more information.[9] However, at the hearing Mr. Williams made numerous adjustments requiring lengthy calculations when provided with documentation and testimony which contradicted the Division's findings, or clarified petitioner's position.[10]

A conciliation conference was conducted in this matter on June 2, 1997. Conciliation Order No.155515, dated September 12, 1997, sustained the statutory notices. A timely petition was filed with the Division of Tax Appeals protesting the notices of determination in issue.

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[9]It is unclear from the record whether these boxes of records related to the test period or the whole audit period.

[10]We modified finding of fact "12" of the Administrative Law Judge's determination to more accurately reflect the record.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

At the outset, the Administrative Law Judge noted that Article 21 of the Tax Law imposes two highway use taxes upon commercial carriers with respect to motor vehicles operated on New York State public highways. The first, the truck mileage tax ("TMT"), is imposed pursuant to Tax Law § 503. This tax is based on the mileage of the vehicle on New York public highways and the weight of the vehicle (20 NYCRR 481.1[a]). The second tax is known as the fuel use tax ("FUT"), and is imposed pursuant to Tax Law § 503-a. The FUT is based upon the amount of motor fuel and diesel motor fuel used in New York. The statute provides for a credit on fuel purchased in New York State but used outside the State (Tax Law § 503-a[3]).

The Tax Law imposes the following record keeping requirements upon carriers:

> Every carrier . . . shall keep a complete and accurate daily record which shall show the miles traveled in this state by each vehicular unit and such other information as the [tax commissioner] may require. Such records shall be kept in this state unless the [tax commissioner] consents to their removal and *shall be preserved for a period of four years* and be open for inspection at any reasonable time upon the demand of the [tax commissioner] (Tax Law § 507, emphasis supplied).

The Division's regulation, in particular, 20 NYCRR 483.4, states in pertinent part:

> Every carrier reporting either under the gross weight or unloaded weight method shall keep available odometer, hubometer and any similar readings, fuel consumption records, map mileage from the point of origin to the point of destination, or tariff schedules or record of mileage used for billing purposes and used to compute the actual taxable mileage which is taxable under article 21 of the Tax Law. The mileage shown in the daily mileage, manifest or trip records, or any other more accurate record for each vehicle, must be the actual mileage traveled and shall be totaled at the end of each month.

The Administrative Law Judge relied on the Court in ***Matter of Lionel Leasing Indus. Co. v. State Tax Commn.*** (105 AD2d 581, 481 NYS2d 520, 523) for guidance concerning the audit standards that must be met. The Court stated:

> Where the taxpayer's records [as required under Article 21] contain substantial discrepancies and there are inadequate or no records, it is impossible to determine petitioner's tax liability without resort to outside indices. The department is required to then select a method of audit reasonably calculated to reflect the taxes due. Petitioner must by clear and convincing evidence demonstrate that the method or the tax was erroneous (***Matter of Urban Liquors v. State Tax Comm.***, 90 AD2d 576, 577, 456 NYS2d 138). Where the taxpayer's record keeping is faulty, exactness is not required of the audit, nor is an item by item analysis necessary (***Matter of Korba v. New York State Tax Comm.,*** 84 AD2d 655, 656, 444 NYS2d 312, [***lv denied*** 56 NY2d 502, 450 NYS2d 1023]). The legislative intent in imposing the highway use tax was to equitably spread the cost of highway maintenance in proportion to the wear and damage caused by the weighted vehicle (***Matter of Consolidated Freightways Corp. of Del. v. Tully***, 89 AD2d 270, 272, 456 NYS2d 457, ***affd*** 59 NY2d 897, 466 NYS2d 317).

The Administrative Law Judge noted that the court's decision in ***Matter of Lionel Leasing Indus. Co.*** (***supra)***, requires the Division to determine a taxpayer's highway use tax liability based upon the taxpayer's records unless those records are inadequate. The court, thus, applied sales tax audit principles to audits conducted under Article 21. Therefore, the Administrative Law Judge found it appropriate to apply the principles governing sales tax audit procedures to the instant matter.

In ***Matter of Chartair, Inc. v. State Tax Commn.*** (65 AD2d 44, 411 NYS2d 41), the court stated:

> Although there is statutory authority for the use of a “test period” to determine the amount of tax due when a filed return is

> incorrect or insufficient (Tax Law § 1138, subd. [a]), resort to this method of computing tax liability must be founded upon an insufficiency of record keeping which makes it virtually impossible to verify taxable sales receipts and conduct a complete audit [citations omitted]. (***Matter of Chartair, Inc. v. State Tax Commn.***, ***supra***, 411 NYS2d, at 43).

The Administrative Law Judge pointed out that since the statutory authority to determine a taxpayer's (sales tax) liability by estimated procedures rests upon first finding that the taxpayer's books and records are inadequate to conduct a complete audit, the Division was required to first request and thoroughly examine the taxpayer's books and records for the entire audit period in order to determine from verification drawn independently from within these records whether they were sufficient to support a complete audit.[11] If, the Administrative Law Judge noted, the Division's examination established that the taxpayer's records are adequate and complete, the taxpayer was entitled to have its assessment calculated based upon a detailed audit of those records. When the taxpayer's records are incomplete and unreliable for determining accurate sales, the Division may resort to a test period.

The Administrative Law Judge noted that a taxpayer can prove that an audit method was not "reasonably calculated to reflect the taxes due" (***Matter of W.T. Grant v. Joseph***, 2 NY2d 196, 159 NYS2d 150, 157, ***cert denied*** 355 US 869, 2 L Ed 2d 75) by showing that records were made available from which the exact amount of tax could have been determined and the Division nonetheless resorted to an indirect audit method (***Matter of Chartair, Inc. v. State Tax Commn.,*** ***supra***).

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[11] ***Citing Matter of Adamides v. Chu***, ***supra***; ***Matter of King Crab Rest. v. Chu***, 134 AD2d 51, 522 NYS2d 978; ***Matter of Christ Cella, Inc. v. State Tax Commn.***, 102 AD2d 352, 477 NYS2d 858; ***Matter of Meyer v. State Tax Commn.***, 61 AD2d 223, 402 NYS2d 74, ***lv denied*** 44 NY2d 645, 406 NYS2d 1025.

In this case, the Administrative Law Judge stated, the TMT assessed is made up of two primary components: the first is a self-assessed portion which resulted from petitioner's failure to properly complete its TMT and FUT returns, where the mileage which was used in the calculation of TMT was reported for purposes of FUT, but not the former. Although petitioner asserted that the TMT was paid at the time of the filing of the returns, the Administrative Law Judge noted that a review of the combined truck mileage and fuel use tax returns covering the audit period and filed by petitioner show either an incomplete calculation of TMT that petitioner neglected to add to the separate calculation of FUT, or a nonexistent calculation of TMT. The Administrative Law Judge concluded that petitioner had not carried its burden of proving it made such payments, or that such payments were made on its behalf. Thus, the Administrative Law Judge sustained this portion of the assessment ($187,646.00). The second component of the TMT assessed was $54,528.00 resulting from the audit results of the test period audit, after adjustments referred to in Finding of Fact "1" of the Administrative Law Judge's determination.

The Administrative Law Judge next discussed the issues concerning the test period audit. In this case, the Administrative Law Judge noted, the audit was commenced by the mailing of an appointment letter which set forth specifically the records which petitioner needed to produce for review by the Division. The Administrative Law Judge stated that one of the critical items needed in an audit of this type was daily records of mileage traveled within the State. The Administrative Law Judge found that this information was not contained in the daily trip reports in enough detail for the Division to calculate the TMT and FUT which petitioner was obligated to pay. Therefore, the Division requested petitioner's ICC travel logs which must be maintained for six months under Federal regulations. The Administrative Law Judge found that the logs

were available only for approximately six months prior to the commencement of the audit in August 1994, which met the Federal requirements. The Administrative Law Judge also pointed out that there is no statute or regulation of New York State that requires the ICC logs be kept by a taxpayer. However, the Administrative Law Judge referred to Tax Law § 507 which requires that records showing miles traveled by a motor carrier on a daily basis must be maintained by the company for four years. A taxpayer operating as a motor carrier must be prepared to calculate actual miles traveled. The Administrative Law Judge stated that where a taxpayer fails to maintain or make available records required under Article 21, the Division is authorized to estimate the taxpayer's highway use tax liability (***see, Matter of Lionel Leasing Indus. Co. v. State Tax Commn., supra***). The Administrative Law Judge found that the Division correctly determined that without the logs or other record of the mileage details that form the basis of the tax in this case, the Division could not have computed the tax due. The Administrative Law Judge then concluded that given the absence of such records, it was not necessary for the Division to conduct a further examination of every component of petitioner's books and records for the entire audit period, only to then reach the same conclusion: petitioner's records were not sufficiently maintained to conduct a complete audit and compute the proper TMT and FUT due.

The Administrative Law Judge concluded the Division was justified in resorting to a test period audit and, given the insufficiency of records for the entire audit period, was not required to obtain petitioner's consent to do so. Despite its authority to resort to an estimated method to compute the tax, the Administrative Law Judge recognized that the Division had a duty to select an audit method reasonably calculated to reflect tax due. There is no presumption of correctness that attaches to the audit unless there is an initial showing that the methodology selected was

reasonably calculated to reflect the tax due (***Matter of Fashana,*** Tax Appeals Tribunal, September 21, 1989). The record must contain sufficient evidence to allow the trier of fact to determine that the audit had a rational basis (***Matter of Basileo***, Tax Appeals Tribunal, May 9, 1991). Once this threshold determination is made, the burden then rests upon petitioner to show by clear and convincing evidence that the methodology was unreasonable or that the amount assessed was erroneous.

The Administrative Law Judge found that the Division chose a quarter within the audit period for which petitioner had complete records, including its ICC logs, so that the audit results would have as its basis petitioner's own records. Petitioner argued that from a statistical perspective, the Division's methodology was unreliable and invalid. In support of petitioner's position, it introduced the testimony of Dr. Moore, whose view was expressed as a pure statistical analysis.

The Administrative Law Judge noted that the primary difference between a test period audit and a statistical sampling audit is that the test period audit generally involves the testing of all records within a portion of an abbreviated audit period, while the statistical method samples randomly-selected items from the entire audit period (***see, Matter of Marine Midland***, Tax Appeals Tribunal, May 13, 1993). The Administrative Law Judge found that since there were critical records missing from prior quarters pertaining to mileage calculations, a statistical sampling in this case would leave the door open for inconsistency and a potentially less reliable result. Had petitioner's records been complete, then the two methods begin from an equal position, the Administrative Law Judge said. However, such was not the case here. Furthermore, the Administrative Law Judge did not consider the factors relied upon by

Dr. Moore as an economistician to necessarily be significant in the analysis of tax matters and audit principles. Thus, the Administrative Law Judge concluded, the test period chosen was the best available method to project the tax liability over the audit period, absent proof by petitioner that it was not representative of a typical period.

Within the test period, a random number of vehicles was chosen to be reviewed in detail. Petitioner argued that the number of vehicles tested was too small, and that the audit result was invalid. However, the Administrative Law Judge noted that where record keeping is inadequate, exactness is not required (***see, Matter of Lionel Leasing Indus. Co. v. State Tax Commn.***, ***supra***), and petitioner must advance more than mere criticism of the Division's audit methodology to prevail on this point.

Although petitioner made the argument that the test period results should be reduced by a credit due to Schuck for an underreporting of fuel purchases, the Administrative Law Judge found that petitioner failed to explain the discrepancy between its records and the lower reported amounts. The Administrative Law Judge concluded that absent substantiation of entitlement to the credit, petitioner's argument was without merit. The Administrative Law Judge found that where petitioner showed the Division that mileage should be adjusted in petitioner's favor due to facts which differed from the Division's assumptions, such adjustments were made. Accordingly, the Administrative Law Judge upheld the additional TMT in the amount of $54,528.00, and FUT in the amount of $49,970.00 resulting from the test period audit, after adjustments.

The Administrative Law Judge noted that the FUT assessment is also made up of two components: $49,970.00 resulting from the test period audit adjustment and $13,686.00 from

MPG adjustments (which decreased MPGs, thereby increasing the amount of fuel required to be used for the same number of miles, resulting in additional FUT). The Division adjusted petitioner's calculation of MPG as reported on its returns if the MPG was over 5.00, claiming reliance on Tax Law § 503-a(2) and 20 NYCRR former 491.3, which stated in pertinent part:

> Where the records of any carrier are inadequate or incomplete the vehicular units of a carrier filing returns shall be deemed to have consumed, on the average, one gallon of diesel motor fuel for every four miles traveled or one gallon of motor fuel for every three miles traveled unless substantial evidence discloses that a different amount was consumed.

Petitioner disagreed with the Division's estimate of MPGs for numerous reasons, all of which the Administrative Law Judge concluded were valid. Additionally, the Administrative Law Judge found that the testimony presented by petitioner provided a basis to consider the reported MPGs as valid. The Administrative Law Judge determined that the portion of the FUT assessed due to MPG adjustments in the amount of $13,686.00 is canceled.

Next, the Administrative Law Judge addressed petitioner's argument that an assessment of TMT and FUT is a violation of the Commerce Clause of United States Constitution, as an unlawful burden on interstate commerce. The Administrative Law Judge noted that although the Division of Tax Appeals may determine whether tax law statutes are constitutional as applied (***see, Matter of David Hazan, Inc.,*** Tax Appeals Tribunal, April 21, 1988, ***confirmed Matter of David Hazan, Inc. v. Tax Appeals Tribunal***, 152 AD2d 765, 543 NYS2d 545, ***affd*** 75 NY2d 989, 557 NYS2d 306), its scope of review does not extend to determining the facial constitutionality of the statutes (***Matter of J.C. Penney Co.***, Tax Appeals Tribunal, April 27, 1989; ***Matter of Fourth Day Enters.***, Tax Appeals Tribunal, October 27, 1988). Here, petitioner

framed its argument in terms of the statute itself being unconstitutional. On that basis, the Administrative Law Judge concluded the Division of Tax Appeals had no jurisdiction to address petitioner's constitutional claim.

The Administrative Law Judge granted the petition to the extent of canceling the assessments of FUT which were based upon the MPG adjustments for the period April 1, 1990 through June 30, 1994, but in all other respects, the petition was denied.

ARGUMENTS ON EXCEPTION

Petitioner on exception challenges the propriety of the test period audit. Petitioner maintains:

a) that the Administrative Law Judge erred in concluding that the test period audit was appropriate, where petitioner had a complete set of books and records for the audit period, and did not consent to a test period audit;

b) that the Division and the Administrative Law Judge improperly failed to provide petitioner a credit for tax payments made by Happiness Trucking, Inc. and T & A Enterprises, Inc.;

c) that the Administrative Law Judge erred when she approved the application of the test period results to the entire audit period, since it is statistically unreliable as demonstrated by the testimony of Dr. Moore;

d) that an audit of 6 vehicles out of 110 is an invalid sample upon which to project the liability in the case;

e) that the decision to use a test period audit without first reviewing the books and records of the taxpayer for adequacy, is in direct conflict with existing law governing such audits; and

f) that the Division improperly refused to review petitioner's boxes of books and records.

Petitioner also continues to argue that the assessment of TMT and FUT is a violation of the Commerce Clause of the United States Constitution, because the tax is an unlawful burden on interstate commerce, and the State has already met its revenue needs by the collection of Thruway tolls.

The Division did not file an exception to the determination of the Administrative Law and elected not to file a brief in opposition.

OPINION

The Administrative Law Judge correctly noted that the Court's decision in ***Matter of Lionel Leasing Indus. Co. v. State Tax Commn.*** (***supra***) requires the Division to determine a taxpayer's highway use tax liability based upon the taxpayer's records unless those records are inadequate. That Court applied sales tax audit principles to audits conducted under Article 21.

The Division, following sales tax principles, may use an indirect audit methodology where the taxpayer's records are so insufficient it is virtually impossible to conduct a detailed audit (***Matter of Chartair, Inc. v. State Tax Commn.*** (***supra***). To determine the sufficiency of the taxpayer's records, the Division must *first* request and thoroughly examine the records provided by the taxpayer for the complete audit period (***Matter of Adamides v. Chu***, ***supra***; ***Matter of King Crab Rest. v. Chu***, ***supra***; ***Matter of Christ Cella, Inc. v. State Tax Commn.***, ***supra***) in order to determine from within these records whether they are sufficient to support a complete audit (***Matter of Meyer v. State Tax Commn***., ***supra***). If the Division determines that the taxpayer's records are adequate and complete, the taxpayer is entitled to have its assessment calculated based upon a detailed audit of its records ***(Matter of James G. Kennedy & Co. v. Chu***,

supra; ***Matter of Chartair, Inc. v. State Tax Commn.***, ***supra***). However, where the initial review of taxpayer's records for the complete audit period results in a finding that they are incomplete and unreliable, the Division may resort to a test period audit ***(Matter of Urban Liqs. v. State Tax Commn.***, ***supra***; ***Matter of Korba v. New York State Tax Commn., supra***), for it is their inadequacy which justifies the use of an indirect audit methodology. An auditor cannot simply ignore a taxpayer's records and conduct such an audit if the records made available do in fact provide an adequate basis on which to determine the amount of tax due (***Matter of Korba v. New York State Tax Commn***., ***supra***).

We reverse, in part, the determination of the Administrative Law Judge.

In this case, neither the audit report nor the testimony of the auditor, Dennis Williams, demonstrates a complete threshold review of petitioner's books and records for the 4-year audit period *prior* to making the conclusion that the taxpayer's records were inadequate.

A review of the audit report and the auditors' contact sheets does not tell us specifically what books and records were provided, specifically what books and records were reviewed, or at what point it was decided that the books and records were determined to be inadequate. Indeed, the auditors' contact sheets seem to reflect a seamless transition from the request for books and records, to the arrival at the audit location and, then, the commencement of a test period audit. Mr. Williams testified that it was Mr. Stewart who made the decision that the books and records were inadequate and to proceed with a test period audit without obtaining an audit method election agreement (Exhibit "G," Hearing Tr., pp. 49-52). However, there is not sufficient evidence in the record to show the process Mr. Stewart followed or the books he reviewed for the 4-year audit period prior to reaching that decision. Mr. Williams' testimony was not helpful in

this regard, since he did not review Mr. Stewart's work, he just picked up where Mr. Stewart left off (***see***, Hearing Tr., p. 52). Mr. Stewart, now retired, did not testify and the Division did not obtain an affidavit from him to show the details of his role in conducting the audit.

The Field Audit Report indicates an audit method election was not offered due to "incomplete records *for the sample period*, as well as the balance of the audit period" (Exhibit "G," p. 2, emphasis added). Mr. Williams was asked what records were not available for the audit period and he replied the "ICC logs" (Hearing Tr., p. 49). Were there any other records that were not available?

> "[W]e do a test period audit so we really don't need four years of records unless there's a problem with that. So normally we just see records for the . . .test period itself, but I believe that the other records were pretty much available" (Hearing Tr., p. 49).

While Mr. Williams testified that the ICC logs were missing for some periods, he also stated at another point that the logs were not always important to the auditors, because they did not provide information that could not be obtained in other documents. So even if the ICC logs were not available for the four year period, some other documents might have been available that would provide the same information. However, without a thorough review of the books and records for the 4-year audit period, the auditors would not know whether such other documents were available or not.

At some point, petitioners offered six file drawers of documents to the auditors for review (***see***, Hearing Tr., pp. 216-217, 410). However, the auditors refused to make even a cursory review of their contents, because someone told them there was no new information in the files. We cannot determine for certain from this record whether these files related solely to the test

period or the whole 4-year audit period. Mr. Williams believed the files were only for the test period. In any event, we find the auditors' refusal to even look at these files inconsistent with sound auditing principles.

Moreover, without an initial review of all of petitioner's books and records for the 4-year audit period, the Division could not make a proper decision as to whether they were inadequate (***see***, ***Matter of King Crab Rest. v. Chu***, ***supra***), and it is their inadequacy which justifies the use of an indirect audit methodology (***see***, ***Matter of Chartair, Inc. v. State Tax Commn.***, ***supra***). Mr. Williams did not have first hand knowledge as to what went into the determination that the records were inadequate, because he did not make that determination, Mr. Stewart did. The audit report does not fill in this factual gap. Since the evidence elicited at hearing fails to demonstrate a sufficient threshold review of petitioner's books and records for the 4-year audit period prior to resorting to a test period audit, we conclude that that portion of the assessment which is based on the test period audit lacks a rational basis.

The TMT assessed herein is made up of two components: the first is a self-assessed portion which resulted from petitioner's failure to properly complete its TMT and FUT returns, where the mileage which was used in the calculation of TMT was reported for purposes of FUT, but not the former. Although petitioner asserts that the TMT was paid at the time of the filing of the returns, the Administrative Law Judge found that the combined truck mileage and fuel use tax returns covering the audit period and filed by petitioner show either an incomplete calculation of TMT that petitioner neglected to add to the separate calculation of FUT, or a nonexistent calculation of TMT. We agree with Administrative Law Judge that petitioner has not carried its

burden of proving it made such payments, or that such payments were made on its behalf. Thus, this self-assessed portion of the assessment (i.e., $187,646.00) is sustained.

The second component of the TMT assessed is $54,528.00 resulting from the audit results of the test period audit. This portion of the assessment is canceled for lack of a rational basis.

The FUT assessment is also made up of two components: $49,970.00 resulting from the test period audit adjustment and $13,686.00 from MPG adjustments (which decreased MPGs, thereby increasing the amount of fuel required to be used for the same number of miles, resulting in additional FUT). The Administrative Law Judge canceled that portion of the FUT assessed due to MPG adjustments in the amount of $13,686.00. Since the Division did not take an exception with respect to this portion of the determination, such conclusion has not been reviewed by us. The portion of the FUT assessment which is based on the test period audit ($49,970.00) is canceled for the reasons set forth above.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Kenneth Schuck Trucking, Inc. is granted to the extent that the portion of the assessment based on the test period audit is canceled, but is otherwise denied;

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

3. The petition of Kenneth Schuck Trucking, Inc. is granted in accordance with the determination of the Administrative Law Judge and with paragraph "1" above, but is otherwise denied; and

4. The Notice of Determination (No. L011671145), dated January 29, 1996, asserting fuel use tax is canceled. The Notice of Determination (No. L011671144), dated January 29, 1996, as modified herein, is sustained for the period April 1, 1990 through June 30, 1994.

DATED: Troy, New York
March 1, 2001

/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