

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition	:	
of	:	
MERRICK DISCOUNT CENTER, LTD. AND KANAT ARBAY, AS OFFICER	:	DETERMINATION
	:	
for Revision of Determinations or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period January 1, 1979 through August 31, 1981.	:	

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Petitioners, Merrick Discount Center, Ltd. and Kanat Arbay, as officer, 75 Taconic Road, Greenwich, Connecticut 06830, filed petitions for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period January 1, 1979 through August 31, 1981 (File Nos. 800362, 800885, 800887, 801114 and 801115).

A hearing was held before Catherine M. Bennett, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on December 7, 1989 at 1:15 P.M., and continued to its conclusion on March 6, 1990 at 2:30 P.M. Petitioners appeared by Jack M. Portney, C.P.A. The Division of Taxation appeared by William F. Collins, Esq. (Irwin A. Levy, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation properly determined additional sales and use taxes due on the gasoline service station operations of petitioner Merrick Discount Center, Ltd.

II. Whether petitioner Kanat Arbay was a person required to collect tax on behalf of the corporate petitioner and is thus liable for unpaid sales and use taxes due.

FINDINGS OF FACT

Petitioner Merrick Discount Center, Ltd. operated a Power Test gasoline station located at 4030 Merrick Road, Seaford, New York, from December 1979 through early August 1981. The station had 16 gasoline pumps and no repair bays. Petitioner Kanat Arbay was president

and owner of Merrick Discount Center, Ltd. (hereinafter referred to as "Merrick").

Initially this case was assigned to Elaine Sullivan, a tax auditor with the Mineola District Office of the New York State Department of Taxation and Finance. Ms. Sullivan made an unannounced visit to the gasoline station located at 4030 Merrick Road in Seaford, New York, on June 21, 1982, at which time petitioner Kanat Arbay was no longer the owner of Merrick Discount Center, Ltd. Ms. Sullivan was informed by the new owner Billur Akdenis that the station had been purchased August 12, 1981 from Kanat Arbay.

She then attempted to contact Mr. Arbay by sending him a notice referred to as a flasher. Subsequently, Frank Gulotta, Mr. Arbay's attorney, contacted Ms. Sullivan. She made an appointment with him on July 28, 1982, which was rescheduled for August 18, 1982, requesting the books and records of the petitioners. Upon arriving at Mr. Gulotta's office on August 18, 1982, Ms. Sullivan was informed that he was cancelling the appointment, that the books and records were at the office of petitioners' accountant and that the accountant would be calling Ms. Sullivan. Upon arriving back at her office, she was informed that Mr. Jack Portney, petitioner's C.P.A., had already personally visited her office in an attempt to speak with her. Ms. Sullivan's testimony revealed that she did not make any further attempt to contact Mr. Portney to acquire books and records of petitioners' service station operations.

Ms. Sullivan further testified that when she visited the gasoline station for the unannounced observation, she took with her an appointment letter requesting books and records. The appointment date was July 12, 1982, and it was addressed to Kaovat Discount Center. She stated that Merrick Discount Center, Ltd. was trading as Kaovat Discount Center, 4030 Merrick Road. On the appointment letter, the request for books and records was as follows:

"All books and records pertaining to your sales tax liability for the period under audit should be available. This would include journals, ledgers, sales invoices, purchase invoices, cash register tapes, exemption certificates and all sales tax records. Additional information may be required during the course of the audit."

There is no further testimony as to what Ms. Sullivan did with that appointment letter. It is not clear whether she subsequently mailed it to Mr. Arbay at the Merrick Road address, gave it to

Mr. Akdenis, or obtained a different address in order to make the request for books and records from petitioners or their representative Mr. Gulotta. It appears that a verbal request for some books and records, for the period June 1, 1979 through February 28, 1982, was made to Mr. Gulotta, but no request was made to Mr. Portney.

Ms. Sullivan proceeded with the audit by obtaining third-party gasoline supplier verification from the Power Test petroleum distributor, the company responsible for supplying Merrick with its gasoline. Having obtained information with respect to the gallons purchased for the period September 1980 through November 1980, Ms. Sullivan calculated estimated taxable sales for that three-month period, and compared that figure to the taxable sales reported on the sales tax returns. An error rate was computed and applied to the total reported taxable sales for the audit period December 1, 1979 through August 31, 1980<sup>1</sup> to arrive at audited taxable sales of \$2,961,329.00. As a result of Ms. Sullivan's calculations, the Division of Taxation issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due to Kanat Arbay, as officer of Merrick Discount Center, Ltd., dated November 20, 1982, in the amount of \$65,538.83,<sup>2</sup> with penalty and interest for a total assessment of \$118,068.87. The periods assessed were as follows:

"As officer of Merrick Discount Center Ltd., you are personally liable under sections 1131(1) and 1133 of the tax law for the following.

<u>Period Ending</u>	<u>Tax Due</u>	<u>Penalty Due</u>	<u>Interest Due</u>
022880	7352.94	3676.47	2517.57
053180	27197.52	13598.76	8489.43
083180	30988.37	15494.19	8753.62"

Ms. Sullivan's testimony indicates that during the course of the audit she was never informed by petitioners' representatives that a significant portion of the gasoline purchased by petitioners was purchased for resale. In fact, when Ms. Sullivan was informed that petitioners'

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<sup>1</sup>Transcript page 22 erroneously describes the audit period as 8/21/81.

<sup>2</sup>Transcript page 22 indicates that the assessment was \$63,538.83.

explanation for the large discrepancy between gasoline purchases and sales reported according to the sales tax returns as filed was due to resale to other gasoline stations, and having been shown copies of sales invoices and resale certificates prepared by petitioners later submitted into evidence, she was not inclined to place much significance on these documents at the time of the hearing.

Sometime after the issuance of the Notice of Determination and Demand for Payment of Sales and Use Taxes Due dated November 20, 1982, petitioners' case was sent to the Special Investigations Bureau for review. Special Investigations made a request for additional records of petitioners. A comparison was made between the gross sales per the Federal income tax returns, the sales tax returns as filed, and the deposits according to the accountant's write-up work. A conclusion was reached that the amounts reported according to the books and Federal returns were approximately 18 times higher than amounts reported on the sales tax returns. Special Investigations also pursued additional third-party verification information from which Ms. Sullivan made further computations and assessments. Gasoline purchases were supplied by the Power Test company for the period December 1979 through August 1981. The taxable gasoline purchases totalled \$2,756,329.00 as compared to the taxable sales reported for the same period of \$162,783.00. The taxable gasoline purchases from the third-party verification information were marked up 15 percent, an estimated markup based on average statewide estimates used during similar audits performed during that time. This resulted in additional sales tax due for the period December 1979 through August 1981 of \$210,489.44. As a result of these calculations, and in accordance with a field audit report prepared by Ms. Sullivan dated January 11, 1984 notices of determination and demands for payment of sales and use taxes due were issued to both Merrick Discount Center, Ltd. and Kanat Arbay as officer on February 24, 1984 assessing tax due of \$81,076.10 with penalty and interest for a total amount of \$150,893.33. The notices contained the following explanation of their assessments:

Merrick Discount Center Ltd.

"The following taxes have been determined to be due in accordance with Section 1138 of the Tax Law, and are based on an audit of your records. In addition, fraud penalties of 50 percent

of the amount of the tax due plus statutory interest have been added pursuant to Section 1145(A)(2).

THE TAX ASSESSED HEREIN HAS BEEN ESTIMATED AND/OR DETERMINED TO BE DUE IN ACCORDANCE WITH THE PROVISIONS OF SECTION 1138 OF THE TAX LAW AND MAY BE CHALLENGED THROUGH THE HEARING PROCESS BY THE FILING OF A PETITION WITHIN 90 DAYS.

<u>PERIOD ENDED</u>	<u>TAX DUE</u>	<u>PENALTY</u>	<u>INTEREST</u>
02/29/80 380	\$ 547.68	\$ 273.84	\$ 284.22
05/31/80 480	2,025.80	1,012.90	986.33
08/31/80 181	2,308.11	1,154.06	1,066.37
11/30/80 281	2,326.87	1,163.44	1,001.26
02/28/81 381	2,430.82	1,215.41	969.76
05/31/81 481	35,378.35	17,689.18	12,979.61
08/31/81 182	36,058.47	18,029.24	11,991.61

NOTE: This assessment is in addition to assessment Nos. S821029034N and S831214006N."

Kanat Arbay  
As Officer

"You are personally liable as officer of Merrick Discount Center Ltd. under Sections 1131(1) and 1133 of the Tax Law for the following taxes determined to be due in accordance with Section 1138(a) of the Tax Law. In addition, fraud penalties of 50 percent of the amount of the tax due plus statutory interest have been added pursuant to Section 1145(A)(2).

THE TAX ASSESSED HEREIN HAS BEEN ESTIMATED AND/OR DETERMINED TO BE DUE IN ACCORDANCE WITH THE PROVISIONS OF SECTION 1138 OF THE TAX LAW AND MAY BE CHALLENGED THROUGH THE HEARING PROCESS BY THE FILING OF A PETITION WITHIN 90 DAYS.

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The field audit report prepared by Ms. Sullivan also indicates that two additional assessments were issued, one to Merrick Discount Center, Ltd. and the other to Kanat Arbay, as officer, in the same amounts assessing tax due of \$63,874.51, with penalty and interest, for a total amount due of \$120,334.87. The notices were dated December 20, 1983 and, according to

the field audit report, assessment numbers S831214006N and S831214007N were issued for the period September 1, 1980 through February 28, 1981 in order to protect the statute of limitations. Although these notices of determination contain the explanation "[s]ince you have not submitted your records for audit as required by Section 1142 of the Tax Law, the following taxes are determined to be due in accordance with Section 1138 of the Tax Law...", there is no testimony as to how these amounts were calculated, whether any records were reviewed or whether petitioners or a representative was consulted.

Executed with respect to taxable period September 1, 1979 through November 30, 1981 was a consent extending the period of limitation for assessment of sales and use taxes under Articles 28 and 29 of the Tax Law allowing appropriate amounts of sales and use taxes to be determined for those periods at any time on or before December 20, 1983. The vendor is identified as Merrick Discount Center, Ltd. and it contains the signature of Jack Portney, C.P.A., petitioners' representative. The Division of Taxation did not produce a consent extending the statute of limitations beyond December 20, 1983.

As Ms. Sullivan indicated by her testimony, at one point in time the file was transferred to the Special Investigations Bureau. There it was handled by Andrew Coughlin who testified that he visited the subject premises on June 7, 1982 viewing eight gasoline pumps and no repair bays. It came to his attention also that the business had been sold during August 1981 and the new owner was Billur Akdenis. Subsequent to his visit to the station, Mr. Coughlin contacted Mr. Gulotta, petitioners' attorney, and visited his office for the purpose of summarizing records in the possession of Mr. Gulotta. Purchases per books were compared to the sales tax returns as filed.

In January 1983, Mr. Coughlin subpoenaed the records representing gasoline purchases by Merrick from Power Test for the period December 1979 through August 12, 1981. Upon receiving the Power Test records, Mr. Coughlin prepared a schedule analyzing the gallons of gasoline purchased and the purchases in terms of dollars. His calculations resulted in potential additional sales tax due of \$180,792.92. It appears, however, that the assessments in issue were

as a result of calculations made by the Mineola District Office and not by Mr. Coughlin.

Jack Portney, certified public accountant, appeared on behalf of petitioners to represent their positions. Mr. Portney testified that Kanat Arbay obtained gasoline not only for his own retail sale purposes but also for resale. He made reference to the fact that Mr. Arbay would pump gasoline from the station during the night when his business was not in operation with a special pump purchased for that purpose. Evidence submitted by Mr. Portney on behalf of petitioners' resale contention included sales invoices covering the period January 1980 through July 1981 showing sales of various types of gasoline to Ahmet Batur at 2 Saratoga Boulevard, Island Park, New York and Apokan Discount, 189 Sunrise Highway, Amityville, New York totalling over \$2,500,000.00. He also submitted the original resale certificates executed by Apokan Discount to Merrick Discount Center, Ltd. dated May 8, 1980 indicating that there was tangible personal property for resale and the resale certificate executed by Ahmet Batur dated February 25, 1980 indicating the same resale activity. Mr. Portney also presented a schedule of purchases of gasoline between January 1980 and July 1981 offset by sales for resale in gallons and dollars as well as retail sales to customers. During the hearing, Mr. Portney clearly indicated that petitioners agree with the Power Test information submitted for the purpose of showing the gallons of gasoline purchased by Merrick. Mr. Portney also submitted correspondence which was a verification from the Heinrich Petroleum Equipment Company, Inc. dated July 10, 1985 stating that Kanat Arbay purchased a Blackmer explosion-proof pump from this corporation during the year 1978 and that since the company was unable to locate the invoice, the letter was being submitted as part of the proof of purchase. Lastly, Mr. Portney submitted into evidence a statement in Turkish which he claims is notarized, as well as bearing an English translation of the same by Abdullah Nevruzhan (whose signature appears on the Apokan Discount resale certificate issued to Merrick) which states as follows:

"I owned several gas stations from 1978 through 1983 and purchased the majority of my gasoline purchases from the gas stations on Long Island owned by Mr. Kanat Arbay, during the above periods my gasoline trucks and drivers would pick up the gasoline at night after the stations had closed by pumping directly from the ground tanks into the truck with portable pumps [sic]. I hope this will clarify [sic] the circumstances regarding my relations with Mr. Kanat Arbay and his gas stations.

Respectfully submitted,

Abdullah Nevruzhan"

It is noted that the statement in the English translation is not dated; however, it does appear that the Turkish copy bears a date stamp and date within the body of the notarization of "19/6/1984".

Mr. Portney, by his testimony, explained that Kanat Arbay was the Turkish ambassador to the State of Pennsylvania and with his political and personal connections was able to obtain large appropriations of gasoline during the 1979 and 1980 gasoline crisis. He further testified that Mr. Arbay had become acquainted with other Turkish people in the gasoline business and assisted them by obtaining large allocations of gasoline which they were unable to obtain directly. He resold substantially all the gasoline he obtained during this period and a very small portion was sold at retail.

#### SUMMARY OF THE PARTIES' POSITIONS

Petitioners do not dispute the gasoline purchases verified by Power Test but submit evidence and contend that a substantial portion of the gasoline so purchased was for resale and that the Division of Taxation's rejection of such evidence is without foundation. Petitioners assert that the Division of Taxation has the responsibility to perform an audit, to review the books and records and make a decision on the basis of the books and records before utilizing outside source information. Petitioners' representative severely criticizes the Division of Taxation and the actions of the auditor who was instructed by an internal memorandum to close out the case on the basis of the records available without further instruction to contact petitioners or their representative.

The Division of Taxation relies on the supplier verification and the computation on that information in its assertion of additional taxable sales. The Division raises the issue that petitioners did not produce witnesses who purportedly were the purchasers of the gasoline resold by Mr. Arbay. The Division characterizes the actions of Mr. Arbay with respect to his ability to obtain large apportionments of gasoline and his choice to deliver to another party as



opposed to selling it himself as senseless. The Division believes that petitioners have not produced sufficient evidence to substantiate the resale contention.

### CONCLUSIONS OF LAW

A. The Tax Law imposes a sales tax on the receipts from the retail sale of tangible personal property (Tax Law § 1105[a]). A "retail sale" is generally defined as a sale of tangible personal property for any purpose other than for resale or for use in a taxable service where the property sold becomes a physical component part of the property serviced or is actually transferred to the purchaser of the service (see, Tax Law § 1101[b][4][i]). A vendor is obligated to maintain records of his sales for audit purposes (Tax Law § 1135) and the Division, when conducting an audit, must determine the amount of tax due "from such information as may be available" but "[i]f necessary, the tax may be estimated on the basis of external indices" (Tax Law § 1138[a][1]). When conducting an audit, the Division of Taxation may not simply ignore a taxpayer's records if those records provide an adequate basis on which to determine the amount of tax due (Matter of Chartair, Inc. v. State Tax Commission, 65 AD2d 44).

To determine the adequacy of the taxpayer's records, the Division must first request and thoroughly examine the taxpayer's books and records for the entire period of the proposed assessment (Matter of King Crab Restaurant v. Chu, 134 AD2d 51). The purpose of this examination is to determine if the records are so insufficient as to make it virtually impossible for the Division to verify taxable sales receipts and conduct a complete audit (Matter of Chartair, Inc. v. State Tax Commission, supra). Considerable latitude is given to the auditor when the taxpayer's records are inadequate. It is only necessary that the Division select an audit method reasonably calculated to reflect the tax due and then it is incumbent upon the taxpayer to establish that the result of the method used is unreasonably inaccurate or that the amount of tax assessed is erroneous (Matter of Meskouris Brothers v. Chu, 139 AD2d 813). In this case, it is unclear whether an adequate request for books was made in the first instance. Apparently, the Special Investigations Bureau was asked to review and investigate the operations of a multitude of gasoline stations during a brief period of time. In addition, an audit was attempted, but

certainly not completed, by the Mineola District Office. Even though it is unclear what records were requested and/or produced, it certainly appears clear from the testimony that the records were not thoroughly examined to determine their adequacy. As a result, the Division of Taxation could not possibly deem the records so insufficient that it was unable to verify taxable sales and conduct a complete audit. The Division of Taxation failed to determine that petitioners' books and records were inadequate, failed to conduct an audit, and it certainly failed to show that the assessment was based on an audit of petitioners' records.

B. If it had been impossible to determine petitioners' tax liability solely from the corporate records, a fact which is not revealed in the record herein, resort to outside indices such as purchases from Power Test was proper (Matter of Urban Liquors, Inc. v. State Tax Commission, 90 AD2d 576; Matter of Cousins Service Station, Inc., Tax Appeals Tribunal, August 11, 1988). It was then the auditor's duty to select a method of audit reasonably calculated to reflect the taxes due (Matter of W. T. Grant Company v. Joseph, 2 NY2d 196, cert denied 355 US 869). In view of the enormous discrepancy between the corporation's reported sales and its purchases per supplier information, the Division was warranted in questioning the adequacy of petitioners' records and giving serious consideration to an estimate based on third-party verification. Even if one argues that the most accurate way to verify taxable sales in this case was by third-party verification, the Division of Taxation simply ignored the resale step of the transaction. The burden was then placed upon petitioners to show by clear and convincing evidence that the audit methodology was unreasonable or that the results obtained were erroneous (Surface Line Operators Fraternal Organization v. Tully, 85 AD2d 858).

C. Mr. Arbay alleges he was able to obtain enormous allocations of gasoline and did so for the purpose of resale to other gas station owners. Although petitioners did not produce witnesses who could speak on their own behalf as purchasers of such gasoline, petitioners were able to produce sales invoices for a substantial portion of the audit period in question. These invoices are supported by resale certificates completed by the parties to whom these sales were made. One of the parties even gave a statement explaining his relationship to Kanat Arbay and

his gasoline purchases. Petitioners further supported their case with information regarding the pump that was purchased for the purpose of pumping gasoline from the delivery site to another tank or truck.

D. Petitioners have met their burden of proving that the results of the investigation and that portion of the "audit" so performed resulted in an erroneous assessment. It is clear in this case that the Division of Taxation performed no review of the books and records and certainly something far less than an audit. The Division also deliberately overlooked records supporting the resale of gasoline by petitioners.

E. It is noted that quarters ended February 29, 1980 through November 30, 1980 as assessed by the notices of determination and demands for payment of sales and use taxes due issued to Merrick Discount Center, Ltd. and Kanat Arbay, as officer, dated February 24, 1984, are beyond the statute of limitations extended by petitioners to December 20, 1983 and therefore must be cancelled.

F. Since it has been determined that there is no liability due, the issue of whether Kanat Arbay was a person required to collect tax need not be addressed.

G. The petitions of Merrick Discount Center, Ltd. and Kanat Arbay are granted and the notices of determination and demands for payment of sales and use taxes due dated November 20, 1982, December 20, 1983 and February 24, 1984 are hereby cancelled.

DATED: Troy, New York

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ADMINISTRATIVE LAW JUDGE