

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
3 GUYS ELECTRONICS, INC.	:	DETERMINATION
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 June 1, 1982	:	
through May 31, 1984.	:	

Petitioner, 3 Guys Electronics, Inc., c/o Intrusco, 312 93rd Street, Brooklyn, New York 11209, filed a petition 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 June 1, 1982 through May 31, 1984 (File No. 801941).

A hearing was held before Robert F. Mulligan, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on July 23, 1987 at 11:00 A.M., with all briefs to be submitted by September 30, 1987. Petitioner appeared by Norman Elias Lahage, P.A. The Audit Division appeared by John P. Dugan, Esq. (Angelo A. Scopellito, Esq., of counsel).

ISSUE

Whether a sales tax audit utilizing gross sales reported on petitioner's Federal income tax return properly determined sales and use taxes due.

FINDINGS OF FACT

1. During the period at issue, petitioner, 3 Guys Electronics, Inc., operated a retail appliance and electronics store at 5423 5th Avenue, Brooklyn, New York. The president of the corporation was Lucien Moughrabie.

2. A sales tax audit of petitioner's books and records was commenced by the Brooklyn District Office in August 1984. (a) Petitioner's books and records were found to be incomplete; no accounting books, cash register tapes or sales slips were produced.

Petitioner had no daily or weekly records. The auditor found that petitioner's accountant had prepared Federal income tax returns from bank statements.

(b) Gross sales per petitioner's Federal income tax returns for the fiscal years ending April 30, 1983 and April 30, 1984 were found to be higher than gross sales reported on petitioner's sales tax returns for the comparable periods by \$117,118.00. The auditor considered the difference to be taxable sales and calculated additional sales tax due based on said amount.

(c) The Federal income tax returns showed furniture and fixtures purchased in 1982 (during the fiscal year ending April 30, 1983) at a cost of \$20,000.00. As petitioner produced no evidence that tax was paid on the purchase of said furniture and fixtures, use tax was determined to be due based on said cost.

3. On February 27, 1985, the Audit Division issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due against petitioner for the period June 1, 1982 through May 31, 1984 in the amount of \$11,312.24 in tax, \$2,284.81 in penalty and \$1,998.87 in interest, for a total due of \$15,595.92.

4. The tax was subsequently reduced to \$9,775.84 on the basis that petitioner had included insurance proceeds of \$18,623.09 in sales on the Federal income tax returns. This reduction was made at a Tax Appeals Bureau conference.

5. The sales tax worksheets of petitioner's accountant show that taxable sales were calculated by taking all bank deposits on petitioner's checking account statements and deducting "Sales Exempted". For example, the amount of "Total Credits" on the May 11, 1982 bank statement (the opening monthly state-ment for petitioner's checking account) shows \$18,962.00. Two deposits, one of \$12,000.00 and one of \$4,000.00, were deducted as capital. The accountant then deducted an additional \$1,000.00 as "Rent," although there was no \$1,000.00 deposit shown in the checking account. The balance remaining, \$1,962.00, was shown as an adjusting entry with the notation "SH." (apparently meaning shortage, as other months carried the reference "Short"). No sales tax return was filed for the quarter ending May 31, 1982. For the quarter ending August 31, 1982, total checking account credits were \$47,202.00. It appears that the prior quarter's shortfall was added to this, with \$3,666.00 in tax and \$3,000.00 in "Rent" being deducted. A "plus" adjusting entry brought total taxable sales to \$44,432.00, with tax of \$3,665.64 (i.e., the \$3,666.00 in tax deducted against deposits for said quarter). This system appears to have been used for all quarters. The adjusting entries, sometimes plus, sometimes minus, varied from quarter to quarter and were not explained in the record.

6. Petitioner's representative claims to have calculated Federal income tax return gross sales figures by using the checkbook credits and maintains that they should not be taken as taxable sales, since numerous items which did not represent taxable sales were included in such deposits. In addition to the insurance proceeds for which petitioner was given credit at the Tax Appeals Bureau conference (Finding of Fact "4"), petitioner's representative argues that the Federal income tax return gross sales figures include export sales, rents, sales tax and returned checks.

7. Through documents and testimony offered at the hearing, petitioner established that the bank deposits included an export sale of \$19,943.38. This sale consisted of shipments of goods to Lebanon, Kuwait and Saudi Arabia. The purchaser paid Mr. Moughrabie personally, as the purchaser knew him but not the "3 Guys" name. The funds were transferred by Mr. Moughrabie from the joint checking account maintained by him and his wife to the corporate checking account.

8. (a) Petitioner claims that rents of \$1,000.00 per month for the building in which petitioner was located were deposited in the corporate checking account and were thus included in Federal gross sales, which constituted the basis of the assessment.

(b) The building was owned by Lucien Moughrabie, not by petitioner, and no rental income was shown on the Federal income tax returns filed by Mr. Moughrabie and his wife.

(c) Petitioner's Federal income tax returns showed no rental income. The return for the

fiscal year ending April 30, 1983 showed a corporate deduction of \$2,843.00 for rent, while the 1984 return showed no rent paid, but a deduction of \$4,300.00 for "Interest on building" and a deduction of \$2,700.00 for real estate tax.

(d) Examination of a rent receipt book offered into evidence by petitioner shows that an average total rental of \$800.00 per month was collected from five tenants. Comparison of the receipt book with the bank statements, however, does not confirm that the funds were deposited in the corporate checking account. If they were so deposited, they were hopelessly commingled with other funds and cannot be identified.

9. While returned checks appear to have been included in the total monthly credits of the bank checking account, there is no evidence that they were included in gross sales on the Federal income tax returns. Gross sales on the Federal income tax returns for the two fiscal years totalled \$376,240.00, while deposit credits per the checking account for the same period totalled \$415,605.00. Thus, \$39,365.00 had been deducted by petitioner in calculating gross sales for the Federal income tax return.

10. There is no evidence to show that sales tax was included in the gross sales as per the Federal income tax returns. As noted in Finding of Fact "9", gross sales per the Federal income tax returns totalled \$39,365.00 less than the checking account credits. This difference is substantially in excess of the \$21,373.00 in sales tax paid with petitioner's returns.

11. As noted in Finding of Fact "2(c)", the Federal income tax returns show \$20,000.00 in furniture and fixtures purchased by petitioner. The sum of \$2,000.00 was deducted in each of the fiscal years ending April 30, 1983 and April 30, 1984 by petitioner. Mr. Moughrabie paid \$2,800.00 for the fixtures when he purchased the building. Additional improvements were subsequently made, such as a dropped ceiling, new lighting and other improvements. The actual cost was said to be unknown. Petitioner's accountant claimed that all except the \$2,800.00 should be treated as nontaxable good will.

CONCLUSIONS OF LAW

A. That Tax Law § 1138(a)(1) provides, in pertinent part, as follows:

"If a return required by this article is not filed, or if a return when filed is incorrect or insufficient, the amount of tax due shall be determined by the tax commission from such information as may be available. If necessary, the tax may be estimated on the basis of external indices, such as stock on hand, purchases, rental paid, number of rooms, location, scale of rents or charges, comparable rents or charges, type of accommodations and service, number of employees or other factors."

B. That where a taxpayer's records are incomplete or insufficient, the Audit Division may select a method reasonably calculated to reflect the sales and use taxes due and the burden then rests upon the taxpayer to demonstrate by clear and convincing evidence that the method of audit or the amount of tax assessed was erroneous

(Surface Line Operators Fraternal Organization, Inc. v. Tully, 85 AD2d 858).

C. That petitioner's records were clearly incomplete and insufficient. Consequently, it was proper for the Audit Division to estimate petitioner's sales pursuant to Tax Law § 1138(a)(1).

The method used by the Audit Division, i.e., to base taxable sales on the gross sales reported on

the Federal income tax returns, was a method reasonably calculated to reflect petitioner's sales and use taxes due.

D. That petitioner has sustained its burden of proof to show that \$19,943.38 represented a nontaxable sale delivered to locations in Lebanon, Kuwait and Saudi Arabia (Finding of Fact "7").

E. That petitioner has failed to sustain its burden of proof to show that anything other than the \$19,943.38 foreign sale (Conclusion of Law "D") and the insurance proceeds (Finding of Fact "4") should not have been included in taxable sales. Petitioner's tangled financial records preclude any other result. Petitioner particularly failed to sustain its burden of proof with respect to the following:

(1) Petitioner has not shown that rental income was included in the Federal gross sales figures used in the assessment. In fact, it appears that petitioner paid rent in the fiscal year ending April 30, 1983 and then took deductions for interest and taxes in the fiscal year ending April 30, 1984, without showing any rental income in either year. Moreover, rental receipts as per the rental receipt book cannot be tied into petitioner's checking account (Finding of Fact "8").

(2) Petitioner has not shown that returned checks were included in Federal gross sales (Finding of Fact "9").

(3) Petitioner has not shown that sales tax was included in Federal gross sales (Finding of Fact "10").

F. That petitioner has not sustained its burden of proof to show that the amount of use tax assessed is incorrect. The fact that petitioner took a depreciation deduction against the \$20,000.00 in furniture and fixtures in the fiscal years ending April 30, 1983 and April 30, 1984 contradicts petitioner's claim that good will was involved. Moreover, petitioner concedes that \$2,800.00 was initially paid for furniture and fixtures and that other improvements of unknown cost were subsequently made.

G. That the petition of 3 Guys Electronics, Inc. is granted to the extent indicated in

Finding of Fact "4" and Conclusion of Law "D". Except as so granted, the petition is denied and the Notice of Determination and Demand for Payment of Sales and Use Taxes Due issued February 27, 1985 is otherwise sustained.

DATED: Albany, New York
February 5, 1988

ADMINISTRATIVE LAW JUDGE