STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition of SOLE TO SOLE, INC. AND ROBIN LONGMATE, AS OFFICER 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 December 1, 1984 through May 31, 1985.	:	DETERMINATION DTA NO. 807925

Petitioners, Sole to Sole, Inc. and Robin Longmate, as officer, 20 Hilton Avenue, Northport, New York 11768, 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 December 1, 1984 through May 31, 1985.

A hearing was held before Arthur S. Bray, Administrative Law Judge at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York on June 12, 1991 at 9:15 A.M. with all briefs to be filed by September 13, 1991. Petitioners filed their brief on August 1, 1991. The Division of Taxation filed its brief on August 30, 1991. Petitioners appeared by Frank Colonna, Jr., C.P.A. The Division of Taxation appeared by William F. Collins, Esq. (Gary Palmer, Esq., of counsel).

ISSUES

I. Whether the audit methodology was reasonably calculated to determine the sales and use taxes due.

II. Whether petitioner Robin Longmate was a person required to collect and pay over sales tax on behalf of Sole to Sole, Inc.

FINDINGS OF FACT

During the period in issue, petitioner Sole to Sole, Inc. (the "corporation") was a firm which operated under the name of Shoe Doctor. It sold prescription orthopedic shoes from a

van which was equipped to enable the operator to obtain the patients' measurements and fittings. The corporation was organized in order to service Medicaid patients.

Mr. Robin Longmate was the corporation's president. During the period in issue, Mr. Longmate's time was consumed in the operations of a company known as Tri Medical Systems, Inc. He was not involved in the daily operations of Sole to Sole, Inc.

The Division mailed a letter dated February 3, 1988 to "Shoe Doctor-Sole to Sole, Inc." which sought to schedule a field audit of the corporation's sales and use tax returns on February 24, 1988. The letter requested that the corporation make available all books and records pertaining to its sales and use tax liability including journals, cash register tapes, Federal income tax returns and exemption certificates.

On February 11, 1988 Mr. Longmate placed a telephone call to the auditor. However, the auditor was unavailable. On February 12, 1988, the auditor and Mr. Longmate spoke. At this time, Mr. Longmate advised the auditor that the firm's records had been taken by the Department of Social Services and that very few of these records had been returned. The auditor was also advised that the business ceased operating in July 1985.

In subsequent telephone calls, Mr. Longmate told the auditor that the business began on February 17, 1985 and continued for five months. On March 1, 1988, Mr. Longmate again stated that he had no records to document sales.

Petitioner Robin H. Longmate, as president, signed a document dated February 21, 1988 which consented to the extension of the period of limitation on assessment of sales and use taxes for the period December 1, 1984 through May 31, 1985 to any time on or before September 20, 1988.

In the course of her audit, the auditor determined that Sole to Sole, Inc. filed two New York State and local sales and use tax returns. One return, for the period December 1, 1984 through February 28, 1985, reported that there were no sales and that no taxes were due. The return was signed by Mr. Longmate as president. The second return was for the period March 1, 1985 through May 31, 1985. The latter return, which was unsigned, reported gross

sales and services of $475,971.00 and taxable sales and services of $19,704.00. It also reported that tax was due in the amount of $1,625.60.

Mr. Longmate wrote a letter to the Division dated June 26, 1985 which set forth the amount of the corporation's gross sales, taxable sales and sales tax collected each month during the three-month period ending May 31, 1985. The letter noted that it included a check in the amount of $1,625.60 for the sales tax collected during the period March 1, 1985 through May 31, 1985.

Since no records were available to conduct an audit, the Division chose to rely on a memorandum in its possession which showed that the New York State Department of Social Services reported payment of $767,331.00 to Shoe Doctor in 1985 on an Internal Revenue Service Form 1099. The Division concluded that since the corporation previously reported taxable sales of $19,704.00, the remainder of $747,627.00 constituted additional taxable sales for 1985. Further, because the corporation did not report any sales during the quarterly period December 1, 1984 through February 28, 1985, the additional gross sales (in excess of the $475,971.00 reported for the quarter ended May 31, 1985) of $291,360.00 were attributed to this period. The Division determined that sales and use tax was due in the amount of $56,072.00 by multiplying the additional taxable sales of $747,627.00 by the tax rate of 7.5 percent.

On the basis of the foregoing calculations, the Division issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due, dated March 4, 1988, to "Shoe Doctor-Sole to Sole, Inc." which assessed sales and use taxes in the amount of $56,072.00, plus penalty of $14,018.00 and interest of $18,584.94, for a total amount due of $88,674.94. The penalty was asserted pursuant to Tax Law § 1145(a)(1) for failure to pay the tax when due. The Division also issued a Notice of Determination and Demand for Payment of Sales and Use taxes Due, dated March 4, 1988, to Robin Longmate as officer of "Shoe Doctor-Sole to Sole, Inc." which assessed the same amount of tax, penalty and interest which had been assessed against the corporation.

A "P. Longmate" signed Postal Service forms 3811, entitled Domestic Return Receipt, showing the receipt of certified mail addressed to, respectively, Shoe Doctor-Sole to Sole, Inc. and Robin Longmate, Officer. Each Domestic Return Receipt showed a delivery date of March 5, 1988. Mr. Longmate's wife is named Patricia.

The corporation's activities with respect to the Medicaid program resulted in Mr. Longmate and his associate, Brian Elenson, being charged with crimes. Ultimately, Mr. Longmate followed his attorney's advice and accepted a plea bargain which required him to perform 280 hours of community service and pay New York State $100,000.00. Mr. Elenson was required to serve time in jail and make restitution in the amount of $150,000.00.

As a result of the criminal investigation, the New York State Attorney General's office acquired possession of Sole to Sole, Inc.'s records. Through their attorney, petitioners made repeated requests for the return of their records. Initially, petitioners were informed that the evidence was still being reviewed. Later, petitioners were advised that the evidence had been returned to Mr. Longmate. Despite the representations of the Attorney General's office, Mr. Longmate denies having received the records.

SUMMARY OF THE PARTIES' POSITIONS

It is petitioners' position that the results of the audit are erroneous because there has never been an examination of petitioners' books and records. Petitioners contend that they were denied access to their records and that the Division should have tried to subpoena the records or use alternative audit methods to verify sales. Relying upon the Field Audit Guidelines, petitioners submit that a sales tax adjustment cannot be based on income reconstruction unless the income reconstruction reveals the source of the error. Petitioners also argue that the sales of orthopedic shoes are not subject to sales tax. However, if there were taxable sales, the amount of taxable sales would be either the $19,704.00 which was reported on the sales and use tax return or the $250,000.00 which was the amount of restitution.

It is also argued that Mr. Longmate is not responsible for the sales and use taxes due because he did not participate in the daily operations of Sole to Sole, Inc. Mr. Longmate

maintains that, despite his title, he had no duty to participate in the business on behalf of the corporation.

It is the Division's position that the unavailability of books and records by reason of their being in possession of another state agency does not excuse the failure to produce books and records for audit. The Division also argues that Mr. Longmate is responsible for the taxes due from Sole to Sole, Inc.

CONCLUSIONS OF LAW

A. Section 1138(a)(1) of the Tax Law authorizes the Division to determine the amount of sales and use taxes due from such information as may be available. If the taxpayer maintains a complete set of books and records, the Division is restricted to the use of those records because "[t]he honest and conscientious taxpayer who maintains comprehensive records as required has a right to expect that they will be used in any audit to determine his ultimate tax liability" (Matter of Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 411 NYS2d 41, 43).

Conversely, the use of external indices is proper when the taxpayer does not produce the records needed to independently determine taxable sales and to conduct an audit (see, Matter of Licata v. Chu, 64 NY2d 873, 487 NYS2d 552; Matter of Club Marakesh v. Tax Commn. of the State of New York, 151 AD2d 908, 542 NYS2d 881, lv denied 74 NY2d 616, 550 NYS2d 276). In order to determine whether a taxpayer's records are adequate to conduct an audit or whether external indices are required, the Division must request and examine the taxpayer's books and records for the entire audit period (Matter of Adamides v. Chu, 134 AD2d 776, 521 NYS2d 826, lv denied 71 NY2d 806, 530 NYS2d 109; Matter of Christ Cella v. State Tax Commn., 102 AD2d 352, 477 NYS2d 858).

B. In this instance, there is no question that the Division requested an opportunity to examine the corporation's records and that the corporation was unable to present those records to the Division. It is petitioners' position that it was incumbent upon the Division to secure the corporation's records from the office of the Attorney General.

C. Tax Law § 1135(d) provides that those required to keep records of sales shall make

such records "available for inspection and examination at any time upon demand". In turn, Tax Law § 1138(a)(1) authorizes the Division to determine tax due when a return is incorrect or insufficient upon "such information as may be available."

In Matter of Continental Arms Corporation v. State Tax Commn. (130 AD2d 929, 516 NYS2d 338, revd 72 NY2d 976, 534 NYS2d 362) the foregoing provisions were central to the ultimate resolution of the proceeding. In that case, the taxpayer's accountant refused to make complete records available to the Division. As a result, the Division conducted a one-month test period audit which led to the issuance of an assessment. Thereafter, the Appellate Division annulled the determination of the State Tax Commission which had sustained the assessment. The Appellate Division reasoned that the use of the test period was improper because the Division could have used its subpoena power to obtain the necessary records (id., 516 NYS2d at 340). On the appeal which followed, the order of the Appellate Division was reversed. After setting forth the foregoing portions of Tax Law §§ 1135(d) and 1138(a), the Court of Appeals held that where a taxpayer refuses to make records available, the Division may use a test period audit and further that the Division is not compelled to resort to its subpoena authority.(Id.) Following the holding in Continental Arms, the Tax Appeals Tribunal recently held in Matter of Morano's Jewelers of Fifth Avenue, Inc. (Tax Appeals Tribunal, January 2, 1992) that the Division was under no obligation to obtain records which were in the possession of the District Attorney in order to conduct an audit.

D. On the basis of Continental Arms and Morano's Jewelers, it is concluded that since the corporation did not present its records for audit, the Division was authorized to use external indices. In addition, the Division was not required to attempt to secure the corporation's records from the Attorney General's office in order to conduct an audit.

E. When the Division uses an indirect audit method, it is required to select a method which is reasonably calculated to reflect the tax due (Matter of W. T. Grant Co. v. Joseph, 2 NY2d 196, 206, 159 NYS2d 150, 157, cert denied 355 US 869, 2 L Ed 2d 75; Matter of Urban Liquors, Inc. v. State Tax Commn., 90 AD2d 576, 456 NYS2d 138, 139). If the Division uses

such a method, the taxpayer bears the burden of proving by clear and convincing evidence that the method of audit or the amount of tax assessed was erroneous (Matter of Surface Line Operators Fraternal Organization, Inc. v. Tully, 85 AD2d 858, 446 NYS2d 451, 453).

F. It is petitioners' position that it was unreasonable to rely on the Form 1099 to calculate the amount of the corporation's sales. This argument is rejected.

G. The regulations promulgated pursuant to the Internal Revenue Code require states to report certain payments on a Form 1099 (Treas Reg § 1.6041-1[g]). Under these circumstances, it was rational for the Division to conclude that the payment represented gross sales. Further, in the absence of any evidence to the contrary, the Division properly determined that all of the receipts were subject to tax (Tax Law § 1132[c]). In reaching this conclusion, it is noted that the Tax Appeals Tribunal has recognized that information on income tax returns is a rational way to estimate taxable sales (see, Matter of William Sidel and Debra Sidel d/b/a Half & Half Trading Co., Tax Appeals Tribunal, July 3, 1991).

H. Petitioners' reliance upon the Division's field audit guidelines to show that the audit method was improper is misplaced. Contrary to petitioners' position, the Division did not attempt to reconstruct petitioners' income. It merely used the Form 1099 to determine the level of petitioners' sales.

I. Tax Law § 1133(a) imposes upon any person required to collect the tax imposed by Article 28 of the Tax Law personal liability for the tax imposed, collected or required to be collected. A person required to collect tax is defined to include, among others, corporate officers and employees who are under a duty to act for such corporation in complying with the requirements of Article 28 (Tax Law § 1131[1]).

J. It is well established that the determination of whether a person is responsible to collect and remit sales tax depends upon the facts of each case (Matter of Cohen v. State Tax Commn., 128 AD2d 1022, 513 NYS2d 564; Stacy v. State of New York, 82 Misc 2d 181, 183, 368 NYS2d 448, 451). The relevant factors to consider when determining whether a person has a duty to act for the corporation are whether the person is authorized to sign the corporation's

tax returns or is responsible for maintaining the corporate books, or responsible for the corporation's management (20 NYCRR 526.11[b][2]). Other factors which have been examined include: the authority to hire and fire employees, the derivation of substantial income from the corporation or stock ownership, and the authority to write checks on behalf of the corporation (see, Matter of Cohen v. State Tax Commn., supra; Matter of Blodnick v. State Tax Commn., 124 AD2d 437, 507 NYS2d 536, appeal dismissed 69 NY2d 822, 513 NYS2d 1027; Matter of Autex Corp., Tax Appeals Tribunal, November 23, 1988). In evaluating the foregoing principles, one must also bear in mind that corporate officials will not be absolved of responsibility by disregarding their duty and relying on others to fulfill their obligations (Matter of Blodnick v. State Tax Commn., supra; Matter of Zefania Baumvoll, as Officer of Jaz Service Center, Inc., Tax Appeals Tribunal, November 22, 1989).

K. In this case, Mr. Longmate argues that he was not a person required to collect tax because he did not take an active role in the management of the corporation and because he was occupied full time in the management of a separate entity.

L. The record shows that Mr. Longmate held the office of president and that he signed documents pertaining to the firm's sales tax liability. On their face, these facts support the position that Mr. Longmate is responsible for the taxes due from Sole to Sole, Inc.

Mr. Longmate's argument does not warrant a different conclusion. At most, it only shows that Mr. Longmate chose to disregard his obligation which, as noted, does not absolve him of responsibility (Matter of Blodnick v. State Tax Commn., supra; Matter of Zefania Baumvoll, as Officer of Jaz Service Center, Inc., supra).

M. The petition of Sole to Sole, Inc. and Robin Longmate, as officer is denied and the notices of determination and demands for payment of sales and use taxes due, dated March 4, 1988, are sustained together with such interest as may be lawfully due.

DATED: Troy, New York

ADMINISTRATIVE LAW JUDGE