

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
HIONAS ENTERPRISES, LTD. AND : **DETERMINATION**
STAMATIOS HIONAS : **DTA NO. 816144**
: :
for Revision of Determinations or for Refund of Sales :
and Use Taxes under Articles 28 and 29 of the Tax Law :
for the Period June 1, 1992 through August 31, 1996. :
:

Petitioners, Hionas Enterprises, Ltd. and Stamatios Hionas, 383 Middle Country Road, Coram, New York 11727, filed a petition for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1992 through August 31, 1996.

A hearing was held before Timothy J. Alston, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on June 11, 1998 at 10:00 A.M., with all briefs to be submitted by October 22, 1998, which date began the six-month period for the issuance of this determination. Petitioner appeared by Milton Shaiman, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Brian J. McCann, Esq., of counsel).

ISSUES

I. Whether, as a result of an audit, the Division of Taxation properly determined additional sales tax due.

II. Whether the Division properly assessed tax due on petitioners' purchases of utilities or whether such purchases were exempt from tax pursuant to Tax Law § 1115(c).

III. Whether the Division properly assessed petitioner Stamatios Hionas as a responsible officer of Hionas Enterprise, Ltd. pursuant to Tax Law §§ 1131(1) and 1133(a).

FINDINGS OF FACT

1. On October 17, 1996, following an audit, the Division of Taxation ("Division") issued to petitioner Hionas Enterprises, Ltd., ("Hionas") a Notice of Determination of sales and use taxes due (notice number L-012801958-3) which assessed a total amount due of \$167,231.90 for the periods June 1, 1992 through August 31, 1992 and June 1, 1993 through August 31, 1996. The total amount due was comprised of \$110,355.81 in tax, plus penalty and interest in the respective amounts of \$30,833.13 and \$26,042.96. The tax assessed against Hionas consisted of \$97,586.22 in tax on additional sales and \$12,769.59 in tax due on utilities purchased by Hionas without payment of tax.

2. During the period at issue, Hionas operated the Coram Pond Diner in Coram, New York. Petitioner Stamatios Hionas was a 50-percent shareholder of the corporation.

Assessment on Additional Sales

3. The Division selected Hionas for audit as part of its BMF (business master file) audit program which compares gross receipts reported by taxpayers on their Federal income tax returns with gross sales reported on their sales tax returns. The Division began the audit by mailing to Hionas a standard form audit appointment letter dated August 6, 1996. In addition to setting a date and time for the first meeting between petitioners and the Division's auditor, this letter advised petitioners to make available on the scheduled date "all books and records pertaining to

your Sales and Use Tax liability for the period under audit.” The letter indicated that the period under audit was June 1, 1993 through May 31, 1996.

4. In response to the Division’s request for records, Hionas produced copies of Federal income tax returns for its fiscal years ended July 31, 1994 and July 31, 1995, and copies of sales tax returns filed during the period at issue. Hionas also produced bank statements, a check disbursement journal, and canceled checks for portions of the years 1994, 1995, and 1996. In addition, Hionas produced a workpaper analysis of such records for its fiscal years ended July 31, 1995 and July 31, 1996 prepared by its accountant. With respect to its fiscal year ended July 31, 1994, Hionas produced bank statements and canceled checks for the months of February, April, May and July 1994.

5. Hionas failed to make available to the auditor any source documentation of its sales. That is, Hionas did not produce any guest checks or cash register tapes. It also did not produce a day book.

6. As noted previously, this audit was part of the Division’s BMF audit program which compares gross receipts as reported on the taxpayer’s Federal return with gross sales as reported on sales tax returns. As part of this program, the Division obtained information contained in the Internal Revenue Service’s computer files regarding Hionas’s Federal income tax return for its fiscal year ended July 31, 1994. This information indicated that Hionas had gross receipts of \$513,259.00 for the year ended July 31, 1994. The Federal income tax return for the year ended July 31, 1994 submitted by Hionas during the audit showed gross receipts of \$450,865.00. In addition to this discrepancy, the return submitted by Hionas claimed a deduction for utilities of \$20,223.00, while the information obtained by the Division from Hionas’s supplier, the Long Island Lighting Company (“LILCO”), indicated utilities purchases of approximately \$47,000.00

during this year. Also, although Hionas submitted a copy of its Federal return for the year ended July 31, 1995, information with respect to this fiscal year was not yet obtainable from the IRS. Accordingly, the Division calculated Hionas's sales tax liability using the information obtained from the IRS with respect to Hionas's Federal income tax return for the year ended July 31, 1994.

7. Specifically, to determine additional tax due on sales, the Division compared gross receipts of \$513,259.00 as reported on Hionas's Federal income tax return for the year ended July 31, 1994 (per information obtained from the IRS) with gross sales as reported on Hionas's sales tax returns for the same period. The Division determined that such gross sales totaled \$323,240.00.¹ Using these figures, the Division calculated a margin of error of 59.143% and applied this error factor to the 14 quarters within the audit period to estimate total audited gross sales of \$1,988,603.00. After allowing for sales tax paid, the Division determined additional tax due on sales of \$97,586.22.

8. At hearing petitioners produced two unsigned Federal income tax returns for the fiscal year ended July 31, 1994, dated October 17, 1994 and August 2, 1996, respectively. The return dated August 2, 1996 had the word "Amended" written across the top. This was the return provided to the Division during the audit, although the copy provided to the Division on audit did not have "Amended" written across the top. The information on the October 17, 1994 return matches the information obtained by the Division from the Internal Revenue Service for the year ended July 31, 1994 (*see*, Finding of Fact "6"). This return lists gross receipts of \$513,259.00. The return dated August 2, 1996 lists gross receipts of \$450,865.00, a difference of \$62,394.00.

¹At the time of the audit, the Division's records indicated that Hionas had failed to file sales tax returns for the periods ended 8/31/92, 2/28/96 and 8/31/96. For these periods the Division estimated reported gross sales using the amount reported for the same quarter during the prior year. For example, the Division deemed Hionas's reported gross sales for the period ended 8/31/91 to be its gross sales for the period ended 8/31/92.

The October 17, 1994 return lists a deduction for salaries and wages of \$164,172.00, while the August 2, 1996 return claims a deduction for salaries and wages of \$101,778.00, also a difference of \$62,394.00. The two returns contain other differences. The October 17, 1994 return claims deductions of \$33,223.00 for utilities, \$11,834.00 for FICA, \$13,810.00 for sales tax, and \$8,352.00 for unemployment insurance. These four deductions total \$67,219.00. The August 2, 1996 return claims deductions of \$20,223.00 for utilities and \$46,996.00 for taxes. These two deductions total \$67,219.00.

9. Petitioners contended that the August 2, 1996 “amended” return was filed with the Internal Revenue Service. Petitioners did not produce any documentary proof of mailing of such return or receipt of such return by the IRS.

10. Petitioners’ representative, a certified public accountant, prepared Hionas’s Federal income tax returns during the period at issue. Petitioners’ representative testified that he calculated Hionas’s gross receipts of \$450,865.00, as reported on the return dated August 2, 1996, using records of bank deposits and a daily log of receipts. Petitioners did not offer into evidence the records purportedly used in the calculation of gross receipts on this return. Petitioners also did not offer any workpapers which may have been used in such calculations.

11. Because Hionas operates a diner, many of its employees receive tips. The employees report their tips to Hionas on payroll forms provided by Hionas. Hionas then forwards these payroll forms to a payroll service. Using the information contained on the payroll forms the payroll service prepares quarterly payroll reports, which lists, among other items, tips reported by Hionas’s employees. Hionas submitted into evidence one such quarterly report dated April 1, 1994. This quarterly report lists tips reported by Hionas’s employees during the first calendar quarter of 1994. The report indicates that such tips totaled \$13,468.44. This amount is the same

as that reported on Hionas's Federal Form 941 (Employer's Quarterly Federal Tax Return) for the first quarter of 1994 according to information obtained by the Division from the Internal Revenue Service.

12. Using the information provided by Hionas's employees, the payroll service also supplied Hionas with completed Tip Reporting Forms (Federal Form 8027). Hionas submitted page 2 of a facsimile of a Form 8027 Tip Reporting Form dated October 21, 1993, which indicates tips reported of \$50,488.41. This document also reports \$1,215.00 in indirect tips, \$50,488.41 in direct tips and total tips of \$51,703.41, but does not indicate the period it purports to cover.

13. Hionas also submitted its Federal Form W-3 (Transmittal of Wage and Tax Statements) for 1994 which indicates "wages, tips, other compensation" of \$163,354.63 and "social security tips" of \$62,394.00. This form was completed using tip information supplied by Hionas's employees.

Assessment on Utilities Purchases

14. By letters dated October 25, 1995 and May 1, 1996 the Division requested that Hionas conduct a self-audit of its utilities purchases and provide the Division with a sampling of its utilities invoices. Hionas did not respond to either of these letters. The Division therefore obtained a record of Hionas's utilities purchases for the period June 1, 1993 through August 31, 1996 directly from its supplier, LILCO. The LILCO records showed that Hionas made utilities purchases totaling \$150,947.00 during that period and that it had not paid any sales tax on its purchases. Accordingly, the Division applied the prevailing sales tax rate to Hionas's utilities purchases and determined total tax due on such purchases of \$12,769.59.

15. Hionas conceded that it had not paid sales tax on its purchases of utilities during the audit period.

16. Hionas had been assessed previously for its failure to pay sales tax on purchases of utilities consumed in its business. The period of this previous assessment was September 1, 1989 through November 30, 1992 and the tax assessed was approximately \$14,000.00. Hionas paid this previous assessment.

Responsible Officer Assessments

17. The Division issued to petitioner Stamatios Hionas (“Mr. Hionas”) four notices of determination of sales and use taxes due as follows:

Notice Date	Assessment No.	Period	Tax Due
October 28, 1996	L-012812074-3	June 1, 1992 - August 31, 1992	\$17,323.92
October 28, 1996	L-012812075-2	Sept. 1, 1992 - August 31, 1996	\$88,281.47
December 30, 1996	L-013052166-5	March 1, 1995 - May 31, 1995	\$ 6,391.49
December 30, 1996	L-013052164-7	March 1, 1996 - May 31, 1996	\$ 5,847.60

18. Each of the four notices informed Mr. Hionas that he was determined to be a corporate officer or a person responsible for the collection and payment of sales and use taxes due from Hionas Enterprises, Ltd. Each notice assessed interest and penalties in addition to the tax due.

19. The assessments dated October 28, 1996 were issued as a result of the field audit of Hionas. That is, the amounts assessed against Mr. Hionas are identical to the tax assessed against the corporation for the same periods. The assessments dated December 30, 1996 were issued by the Division’s Compliance Division in response to the corporation’s failure to file sales tax returns or remit tax.

20. Mr. Hionas's first protest of the assessments numbered L-012812074-3, L-013052166-5 and L-013052164-7 was made through the filing of the petition in this matter on October 3, 1997. Petitioner did not file any protest of these three assessment before that time.

21. Mr. Hionas offered no evidence to show that he was not a person responsible for the collection and payment of sales and use taxes due from Hionas Enterprises, Ltd.

22. The Division submitted copies of documents described as certified mail logs purporting to show that the Division issued the assessments listed above to Mr. Hionas on October 28, 1996 and December 30, 1996, respectively. The Division did not offer any evidence of its standard mailing procedures or any evidence to explain the certified mail logs.

Adjustments to Assessments

23. Following a Bureau of Conciliation and Mediation Services conference, the Division canceled the assessment for the period June 1, 1992 through August 31, 1992 for both the corporation and Stamatios Hionas. The Division also adjusted the assessment for the period March 1, 1996 through May 31, 1996 because of a previously issued assessment for this period. Specifically, the corporation had filed a return for this period without payment. The Division's Compliance Division had issued an assessment against the corporation in the amount of the tax reported due on that return. The Division had not accounted for this prior assessment in issuing assessment numbers L-012801958-3 and L-012812075-2. Accordingly, tax assessed as a result of the audit herein for the period ended May 31, 1996 was reduced from \$10,040.08 to \$4,192.08.

24. The foregoing adjustments were reflected in a Conciliation Order dated September 26, 1997 issued to the corporation which recomputed the tax assessed in notice number L-012801958-3 to \$87,167.15.

CONCLUSIONS OF LAW

Assessment on Additional Sales

A. As a vendor of food and beverages, Hionas was responsible for collecting sales tax on its retail sales (*see*, Tax Law §§ 1105[d][i]; 1132[a]). Hionas was also obligated to keep records of every sale and the tax due thereon, including “a true copy of each sales slip, invoice, receipt, statement or memorandum” (Tax Law § 1135[a]) upon which the sales “tax shall be stated, charged and shown separately on the first of such documents given to (the purchaser)” (Tax Law § 1132[a]). Failure to maintain and make such records available, or the maintenance of inadequate records, authorizes the Division of Taxation to estimate tax liability on the basis of external indices (Tax Law § 1138[a][1]). Here, Hionas failed to maintain or make available upon the Division’s clear request any source documentation of its sales, such as guest checks or cash register tapes. The Division was therefore authorized under Tax Law § 1138(a)(1) to estimate the corporation’s sales tax liability.

B. Where the Division seeks to estimate a taxpayer’s sales tax liability on the basis of an indirect audit method, the methodology selected must be reasonably calculated to reflect the taxes due (*Matter of Ristorante Puglia, Ltd. v. Chu*, 102 AD2d 348, 478 NYS2d 91, 93; *Matter of W. T. Grant Co. v. Joseph*, 2 NY2d 196, 159 NYS2d 150, 157, *cert denied* 355 US 869) but exactness in the outcome of the audit method is not required (*Matter of Markowitz v. State Tax Commn.*, 54 AD2d 1023, 388 NYS2d 176, 177, *affd* 44 NY2d 684, 405 NYS2d 454; *Matter of Lefkowitz*, Tax Appeals Tribunal, May 3, 1990). The burden rests with the taxpayer to show by clear and convincing evidence that the methodology was unreasonable or that the amount assessed was erroneous (*Matter of Meskouris Bros. v. Chu*, 139 AD2d 813, 526 NYS2d 679;

Matter of Surface Line Operators Fraternal Org. v. Tully, 85 AD2d 858, 446 NYS2d 451, 452).

C. In this case, the Division estimated tax due on the basis of a Federal income tax return filed by Hionas for the year ended July 31, 1994. A comparison of the sales tax returns and the Federal return for this one-year test period revealed a significant discrepancy in reported Federal gross sales and reported gross sales per the sales tax returns. This discrepancy was translated into an error rate which was then applied to all of the corporation's reported gross sales to determine additional sales subject to tax. In light of the absence of any source documentation of sales, the audit method resorted to by the Division was reasonable. Moreover, the use of gross receipts as reported on Federal income tax returns to estimate taxable sales has been found to be reasonable in similar situations (*see, e.g., Matter of Scotto*, Tax Appeals Tribunal, January 16, 1992; *Matter of Sidel*, Tax Appeals Tribunal, July 3, 1991).

D. Petitioners have not shown that the audit method employed was unreasonable or that the amount assessed was erroneous. Hionas's claim that the audit methodology was unreasonable and the audit result erroneous is premised on its contention that \$513,259.00 reported as gross receipts on its Federal income tax return for the year ended July 31, 1994 dated October 17, 1994 erroneously included tips received by its employees. Hionas further contends that this error was corrected by the return dated August 2, 1996 which made the appropriate adjustments to its reported gross receipts and wages for the year ended July 31, 1994. Hionas further asserts that the amended return was filed with the Internal Revenue Service.

Hionas's claim is rejected. Hionas failed to show that its gross receipts for the year ended July 31, 1994 were correctly reported as \$450,865.00 on the amended return. Hionas's representative testified that gross receipts of \$450,865.00 as reported on the amended return were

calculated using records of bank deposits and daily logs. Hionas did not, however, submit such records in evidence. Absent any supporting documentation, Hionas has clearly failed to prove that its gross receipts for the the year ended July 31, 1994 were \$450,865.00.

Hionas also failed to show that gross receipts as reported on the return dated October 17, 1994 improperly included tips received by its employees. Although, as noted, Hionas's representative testified that gross receipts for Federal income tax purposes were calculated using records of bank deposits and daily logs, Hionas failed to offer any explanation (other than carelessness) as to how the tips came to be included in gross receipts on the original return. Hionas did offer evidence of the amount of tips reported by its employees (*see*, Findings of Fact "11", "12" and "13"). The fundamental point Hionas needed to prove, however, was not whether its employees reported \$62,394.00 in tips during the year in question, but whether tips were erroneously included in the calculation of gross receipts on the October 17, 1994 return. Petitioners failed to prove this point.

Also weighing against Hionas's contention is its failure to prove that it filed the "amended" return dated August 2, 1996 with the Internal Revenue Service. Hionas relied heavily on its contention that it filed this return to establish the validity of its claim. The record does not support this contention. Petitioners did not produce any documentary proof of mailing of this return, such as a certified mail receipt. Petitioners' representative explained this circumstance by his testimony that he mailed the amended return by ordinary mail. Petitioners also did not produce any documentary evidence of receipt of the amended return by the IRS, although petitioners' representative conceded that such proof was readily obtainable. This point is significant considering that petitioners were aware prior to the hearing that the Division had not accepted the claimed amended return, instead using the information obtained from the IRS which

was in turn taken from the October 17, 1994 return. Since Hionas sought to establish the validity of the figures on the amended return by asserting the fact of its filing with the IRS, it seems incongruous that it would not have sought to obtain proof from the IRS of such filing. Under these circumstances the uncorroborated testimony of petitioners' representative that he filed the "amended" return is insufficient to prove that this return was filed.

Accordingly, since petitioners failed to show that gross receipts as reported on the October 17, 1994 return were in error and the gross receipts as reported on the August 2, 1996 return were correct, there is no basis to adjust or modify the results of the Division's audit of the corporation's sales.

Assessment on Utilities Purchases

E. Hionas did not take issue with the Division's calculation of tax due on its utilities purchases; rather, Hionas contended that such purchases were properly exempt from sales tax pursuant to Tax Law § 1115(c), which exempts sales of gas and electricity used or consumed "directly and exclusively in the production of *tangible personal property* . . . for sale (italics added)." This contention is rejected. The sale of food or drink in or by a restaurant, such as the diner operated by Hionas, is subject to tax under Tax Law § 1105(d)(i). Food or drink sold subject to tax under Tax Law § 1105(d)(i) is not tangible personal property (*Matter of Burger King, Inc. v. State Tax Commn.*, 51 NY2d 614, 621, 435 NYS2d 689, 691). Accordingly, the corporation's purchases of utilities were not eligible for the production exemption of Tax Law § 1115(c). (*See also, Marriott Family Restaurants, Inc. v. Tax Appeals Tribunal*, 174 AD2d 805, 570 NYS2d 741, *lv denied* 78 NY2d 863, 578 NYS2d 877.)

Responsible Officer Assessments

F. Tax Law § 1133(a) imposes personal liability for sales and use tax imposed, collected, or required to be collected under Article 28 of the Tax Law upon persons required to collect tax. Tax Law § 1131(1) defines such “persons” as including “any officer, director or employee of a corporation or of a dissolved corporation . . . who as such officer, director or employee . . . is under a duty to act for such corporation . . . in complying with any requirement of [Article 28].”

Petitioners contended that the assessment against Mr. Hionas was improper because “there should have been a formal hearing to establish that Mr. Hionas was a responsible party” (Petitioners’ brief). Petitioners also contended that Mr. Hionas was improperly assessed amounts which were not trust fund monies (i.e., tax on purchases of utilities). For its part, the Division contended that Mr. Hionas’s protest of assessment numbers L-012812074-2, L-013052166-5, and L-013052164-7 is barred by Tax Law § 1138(a)(1), which provides for a 90-day period to challenge a notice of determination.

Addressing the Division’s contention first, where the Division alleges that a taxpayer’s protest is untimely, it bears the burden of demonstrating proper mailing (*see, Matter of Katz*, Tax Appeals Tribunal, November 14, 1991). The Division may meet this burden by evidence of its standard mailing procedure, corroborated by direct testimony or documentary evidence of mailing (*see, Matter of Accardo*, Tax Appeals Tribunal, August 12, 1993). In this case, the Division has not presented any evidence of its standard mailing procedures. Nor has the Division presented any evidence to explain the certified mail logs it introduced into the record. The Division has thus clearly failed to meet its burden. Accordingly, the Division’s assertion that Mr. Hionas’s protest of these assessments was untimely is rejected.

Turning next to petitioners’ contentions, the Division of Taxation does not have the burden of proving the propriety of its assessment (*see, Matter of A & J Gifts Shop v. Chu*, 145

AD2d 877, 536 NYS2d 209, *lv denied* 74 NY2d 603, 542 NYS2d 518), for a presumption of correctness attaches to a notice of determination upon its issuance (*see, Matter of Hammerman*, Tax Appeals Tribunal, August 17, 1995), and the burden of proving an assessment erroneous rests with the taxpayer (*see, Allied New York Services v. Tully*, 83 AD2d 727, 442 NYS2d 624). A taxpayer who fails to present any proof as to the incorrectness of a determination surrenders to the presumption of correctness (*see, Matter of Tivolacci v. State Tax Commn.*, 77 AD2d 759, 431 NYS2d 174, 175). Here, Mr. Hionas presented no evidence at the hearing to show that he was not a responsible officer of the corporation. Accordingly, the assessments against petitioner Stamatios Hionas must be sustained.

Petitioners' contention that "there should have been a formal hearing to establish that Mr. Hionas was a responsible party" overlooks the fact that the hearing in this matter was such a "formal hearing" and that such hearing was Mr. Hionas's opportunity to show that he was not a responsible officer. Contrary to petitioners' apparent suggestion, there is no provision in the Tax Law for a hearing to determine an individual's responsible officer status prior to the issuance of a statutory notice.

As to Mr. Hionas's other contention, it is well established that the liability of responsible officers under Tax Law § 1133(a) extends to tax due on purchases made by the corporation (*see, Matter of Laschever*, Tax Appeals Tribunal, March 23, 1989). The Division's assertion of tax due from Mr. Hionas arising from the corporation's purchases of utilities was therefore proper.

G. The petition of Hionas Enterprise, Ltd. and Stamatios Hionas is in all respects denied and the notices of determination numbered L-012801958-3, L-012812074-2, L-012812075-2, L-013052166-5, and L-013052164-7, as modified in accordance with Findings of Fact "23" and

“24”, are sustained. Also in accordance with Finding of Fact “23”, the Notice of Determination numbered L-012812074-3 is canceled.

DATED: Troy, New York
April 1, 1999

/s/ Timothy J. Alston
ADMINISTRATIVE LAW JUDGE