STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions	:	
of	:	
AERO SERVICES INTERNATIONAL, INC.	:	DETERMINATION DTA NOS. 817801,
for Redetermination of Deficiencies or for Refund of Tax on Petroleum Businesses under Article 13-A of the Tax Law for the Period September 1, 1991 through November 30, 1993.	:	817802, 817803, 817804, 817805, 817806, 817807 AND 817808
	:	

Petitioner, Aero Services International, Inc., 660 Newtown-Yardley Road, Newtown, Pennsylvania 18940, filed petitions for redetermination of deficiencies or for refund of tax on petroleum businesses under Article 13-A of the Tax Law for the nine quarterly periods from September 1, 1991 through November 30, 1993.

On April 12, 2001 and April 16, 2001, respectively, petitioner, by its representative, Robert Abrams, Esq., and the Division of Taxation by Barbara G. Billet, Esq., (John E. Matthews, Esq., of counsel) consented to have this controversy determined upon a stipulation of facts and the submission of documents without hearing. All briefs were to be submitted by July 18, 2001, which date began the six-month period for the issuance of the determination. After due consideration of the entire record, Gary R. Palmer, Administrative Law Judge, renders the following determination.

ISSUES

I. Whether petitioner is subject to additional tax due on petroleum businesses pursuant to Article 13-A of the Tax Law.

II. Whether the statute giving rise to petitioner's asserted Article 13-A liability is either facially unconstitutional or unconstitutional as applied to petitioner's circumstances.

III. Whether petitioner is subject to either fraud penalty or penalty for failure to pay the tax on petroleum businesses.

FINDINGS OF FACT

1. Petitioner, Aero Services International, Inc. ("Aero"), and the Division of Taxation ("Division") entered into a Stipulation of Facts which has been substantially adopted as Findings of Fact "2" through "11". Attached to the Stipulation are certain documents referenced in the Stipulation and submitted by the joint agreement of the parties, which documents include a schedule referring to and incorporating information from the nine notices of determination issued by the Division.

2. During the audit period petitioner was registered with the Department of Taxation and Finance as a fixed base operator ("FBO") and was engaged in the sale of kero-jet fuel from its business location at the Westchester County Airport in White Plains, New York ("New York FBO").

3. From the late 1940s through the mid 1980s petitioner prospered in its operation of 20 FBOs, including the New York FBO, which were located in various parts of the United States. The on-site management at these locations generally operated these facilities with a great deal of autonomy from petitioner's corporate headquarters located in Newtown, Pennsylvania.

4. An Article 13-A petroleum business tax audit of petitioner's New York FBO was commenced in September 1994, by the issuance of an appointment letter from the Division's Capital Region District Office. The appointment letter included a request for all relevant books

and records including exemption and resale certificates. Further such requests for relevant books and records were made by the auditor during the course of the audit and during field visits. All records produced by petitioner were examined. The records produced by petitioner included copies of tax returns, purchase invoices, computerized sales reports, credit card receipts and fuel cost forms. Of these records, the fuel cost forms were obtained from the New York FBO and the remaining records came from petitioner's Newtown, Pennsylvania corporate headquarters. No exemption or resale certificates were provided to the Division at any time during the audit.

5. The Division's auditor examined petitioner's petroleum business tax ("PBT") returns for the audit period (Forms PT-200, PT-202 and supporting schedules). This examination revealed that all gallons of kero-jet fuel sold during the audit period were reported on line 8 of each Form PT-202 as "[s]ales to persons registered as aviation fuel businesses or under 12A or to United States government, New York State and its municipalities, or consumed by you in your aircraft." On line 13 of each Form PT-202 petitioner reported that none of the gallons of kero-jet fuel were consumed by petitioner in its own aircraft. On the PBT returns for each quarter at issue petitioner reported no taxable sales and paid only the minimum petroleum business tax of $75.00 per quarter. Petitioner's total reported volume of nontaxable sales for the audit period was 5,844,662 gallons. Nine notices of determination were issued to petitioner. Relevant portions of the schedule of sales by quarter with associated tax, penalty and interest due are reproduced below.

Notice #	q/e Date	Gallons	Tax rate	Tax paid	Add'l tax due	Penalty	Interest	Total
41213PP01	11/30/91	638,208	0.1277	$75.00	$81,424.16	$79,723.98	$78,023.80	$239,171.94
50307PP01	02/29/92	575,281	0.1277	75.00	73,388.38	70,202.20	67,016.01	210,606.59
50602PP01	05/31/92	640,879	0.1484	75.00	95,031.44	89,037.51	83,043.57	267,112.52
50912PP01	08/31/92	643,011	0.1484	75.00	95,347.83	87,550.87	79,753.91	262,652.61
51212PP01	11/30/92	738,338	0.1484	75.00	109,494.36	98,720.20	87,946.04	296,160.60

60301PP01	02/28/93	590,261	0.1484	75.00	87,519.73	77,557.72	67,595.71	232,673.16
60612PP01	05/31/93	711,354	0.1484	75.00	105,489.93	91,847.68	78,205.43	275,543.04
60904PP01	08/31/93	696,730	0.1484	75.00	103,319.73	88,385.01	73,450.28	265,155.02
61213PP01	11/30/93	610,600	0.1484	75.00	90,538.04	76,111.01	61,684.12	228,333.24
Totals		**5,844,662**		**$675.00**	**$841,553.60**	**$759,136.24**	**$676,718.87**	**$2,277,408.71**

6. The on-site manager of the New York FBO used internal pricing sheets ("fuel cost forms") to determine the price he would charge for fuel. The manager reviewed such completed fuel cost forms with the vice president responsible for oversight of the New York FBO who, during the audit period, was located in Houston, Texas. The fuel cost forms were not submitted to petitioner's headquarters in Newtown. The vice president in Houston simply provided the accounting department in Newtown with summaries of the fuel cost forms detailing the total sales price and selling volume for the New York FBO. These summaries were utilized by the accounting department to prepare and file the petroleum business tax returns at issue herein.

7. The auditor verified the retail selling price for each quarter by reference to petitioner's quarterly sales reports.

8. Petitioner purchased the fuel at issue from Exxon Company, USA, paying to Exxon the base price for the fuel plus Federal excise tax, New York State prepaid sales tax and an airport fee.

9. Coopers & Lybrand was petitioner's public accounting firm for the audit period. As part of its annual audit for petitioner, a copy of the report of which was filed each year as a public record with the U.S. Securities and Exchange Commission, Coopers & Lybrand would send a state tax expert to petitioner's headquarters in Newtown for several days each year to review petitioner's performance and records for compliance with state tax statutes and regulations including the petroleum business tax. Petitioner's management was never advised by Coopers & Lybrand of any failure to comply with any of New York's tax laws.

10. On May 20, 1994, subsequent to the sale of the New York FBO and four months prior to the initiation of the Division's audit, the current management team was put in place when Triton Energy Corporation, petitioner's principal shareholder, concluded the sale of its interests in petitioner to Transtech Holding Co., Inc. Since the Coopers & Lybrand audits of petitioner never disclosed any unpaid New York taxes, Transtech was unaware that any such liability existed at the time it purchased Triton's holdings in petitioner.

11. The parties have stipulated that in the event the Division is unable to meet its burden to prove its entitlement to fraud penalty, then the Division will bear the burden to prove the absence of reasonable cause in order to sustain the penalty for failure to pay imposed by Tax Law § 289-b(1)(a).

12. The fuel cost forms provided to the Division revealed that the retail selling price of each gallon of kero-jet fuel included the Article 13-A gross receipts tax as a separate line item.

13. The kero-jet fuel sold by petitioner to its customers and pumped by it into the fuel tanks of its customers' aircraft was, prior to the sale, removed from storage facilities at the Westchester County Airport owned by Exxon Company USA or petitioner.

14. A narrative report prepared by Division audit personnel referenced the statement of Wally Sipe, who formerly served as the general manager of the New York FBO and whose duties included the preparation of the fuel pricing sheets. Mr. Sipe's statement, as recounted in the narrative report, reads, "that the home office was aware of the Tax Law and that all sells [sic] were taxable."

CONCLUSIONS OF LAW

A. The parties stipulated to petitioner's status as a registered New York State Fixed Base Operator ("FBO") engaged in the sale of kero-jet fuel. The term Fixed Base Operator is defined in Tax Law § 282(17) as "any . . . corporation . . . which engages in the sale of kero-jet fuel or aviation gasoline, or both, for airplanes from a fixed and permanent place at an airport within the state." Tax Law § 282-a(2) of Article 12-A provides that, "[t]he commissioner may . . . register as a distributor of kero-jet fuel only a fixed base operator who makes no sales of kero-jet fuel other than retail sales not in bulk delivered directly into the fuel tank of an airplane . . . and who makes no other sale of diesel motor fuel." Tax Law § 300(b)(2) defines the term "petroleum business" with respect to diesel motor fuel to include, "every corporation . . . registered by the department of taxation and finance as a 'distributor of kero-jet fuel only' pursuant to the provisions of subdivision two of section two hundred eighty-two-a of this chapter." Tax Law § 302(a) mandates that each petroleum business with respect to diesel motor fuel register under Article 12-A as a distributor of diesel motor fuel or as a distributor of kero-jet fuel only.

For the period beginning September 1, 1990 Tax Law § 301-a(a) imposes on "every petroleum business for the privilege of engaging in business, doing business, employing capital, owning or leasing property, or maintaining an office in this state, a monthly tax for each or any part of the taxable month . . ." as thereinafter computed. The Commissioner of Taxation and Finance is authorized to permit the filing of petroleum business tax returns on a quarterly basis in the case of a petroleum business registered as a distributor of kero-jet fuel only (Tax Law § 308[a]). Tax Law § 308(a) reflects the change effective September 1, 1990 in the Article 13-A tax from an annual gross receipts tax to a monthly or quarterly gallonage tax.

Petitioner, as a registered distributor of kero-jet fuel only, meets the Tax Law § 300(b)(2) definition of a petroleum business. As a petroleum business doing business, leasing property or maintaining an office within New York State, petitioner is subject to the petroleum business tax imposed under Article 13-A.

B. Petitioner, in its brief, contends that Tax Law § 301(a)(1)(iii) is unconstitutional on its face and as applied and, as a consequence, the statutory notices are subject to cancellation. In support of its facially unconstitutional argument, petitioner cites to ***Matter of Tug Buster Bouchard Corporation v. Wetzler*** (217 AD2d 192, 635 NYS2d 803, ***affd*** 89 NY2d 830, 653 NYS2d 271), which found that Tax Law § 301(a)(1)(ii) was facially discriminatory in that it imposed an impermissible burden on interstate commerce. Petitioner opines that because section 301(a)(1)(ii) is drafted similarly to section 301(a)(1)(iii) (which applied to aviation fuel), there is a great likelihood that section 301(a)(1)(iii) would be found to be unconstitutional too. Because the audit period herein began on September 1, 1991 and Tax Law § 301(a)(1)(iii) was not in force after August 31, 1990, the focus of this inquiry should be on Tax Law § 301-a(a) which became effective on September 1, 1990 (***see,*** L 1990, ch 190, § 216).[1] Presuming that it was petitioner's intention to assert that it is Tax Law § 301-a that violates the Commerce Clause of the United States Constitution and that petitioner's reference to the facial unconstitutionality of section 301(a) was erroneous, and because the Division of Tax Appeals is without jurisdiction to determine facial constitutionality as it is without jurisdiction to review an act of the Legislature (***Matter of Unger,*** Tax Appeals Tribunal, March 24, 1994), the focus of this review will turn to

[1] The audit period covered by ***Tug Buster Bouchard Corporation v. Wetzler (supra)*** is from January 1984 to August 1990.

petitioner's challenge to the statute's constitutionality as applied to petitioner's circumstances.

C. In its reply brief petitioner sought to distinguish its circumstances from those of the petitioner in ***Matter of Consolidated Rail Corporation v. Tax Appeals Tribunal*** (231 AD2d 140, 660 NYS2d 459), wherein that petitioner charged that Tax Law § 301-a facially discriminated against interstate commerce. The Appellate Division held that section 301-a did not offend the Commerce Clause on its face in that the taxable event was the withdrawal of the diesel motor fuel from storage in New York for use in the petitioner's locomotives, which storage served to place the fuel beyond the stream of interstate commerce. In support of its "as applied" challenge in its reply brief, petitioner in this matter, while conceding that the kero-jet fuel "may have been at rest while in the fuel tank farms of Exxon, [the fuel] ceased to be at rest once pumped into the fuel trucks of [petitioner] for immediate dispersal into the tanks of private and commercial carriers." Petitioner argues that, unlike the ***Consolidated Rail*** case, "[t]here is no storage issue here . . ." because it purchased the fuel from Exxon to sell to airlines and airline operators for their immediate consumption. This, claims petitioner, caused the fuel to enter the stream of interstate commerce so that New York could not impose the petroleum business tax without placing an impermissible burden on interstate commerce. Petitioner has not shown specific facts in the record which serve to demonstrate that section 301-a discriminates only in its application to petitioner. There is no showing, for example, why the purported burden to interstate commerce that comes into play when petitioner withdraws the fuel from storage at the Westchester County Airport and dispenses it into the fuel tanks of its customers' aircraft for immediate use, does not affect all other New York fixed base operators in the same manner. Clearly, this aspect of petitioner's challenge is to the facial constitutionality of section 301-a as

opposed to a form of discrimination that applies uniquely to petitioner (***see, Matter of Texas Eastern Transmission Corp.,*** Tax Appeals Tribunal, November 12, 1998, ***confirmed*** 260 AD2d 127, 699 NYS2d 560, ***affd*** 95 NY2d 323, 717 NYS2d 69). Because legislative enactments are presumed to be constitutional at the administrative level, the merits of this issue are determined to be in keeping with that presumption.

D. Tax Law § 289-b(1)(d) of Article 12-A provides:

> If the failure to pay any tax within the time required by or pursuant to this article is due to fraud, in lieu of the penalties and interest provided for in paragraphs (a) and (b) of this subdivision, there shall be added to the tax (i) a penalty of fifty per centum of the amount of tax due, plus (ii) interest on such unpaid tax at the underpayment rate set by the commissioner of taxation and finance . . . plus (iii) . . . an amount equal to fifty per centum of the interest payable under subparagraph (ii) of this paragraph on that portion of the unpaid tax which is attributable to fraud.

In ***Matter of Wisdom*** (Tax Appeals Tribunal, November 12, 1998), it was held that the penalty provisions of Tax Law Article 12-A are applicable to Article 13-A by operation of Tax Law § 315(a).

E. The Division has the burden of proving fraud by clear and convincing evidence which establishes "willful, knowledgeable and intentional wrongful acts or omissions constituting false representations resulting in deliberate nonpayment or underpayment of taxes due and owing" (***Matter of Ilter Sener d/b/a Jimmy's Gas Station,*** Tax Appeals Tribunal, May 6, 1988). Willful intent is a critical element of fraud. It must be proven that the taxpayer "acted deliberately, knowingly, and with the specific intent to violate the Tax Law" (***Matter of Cousin's Service Station, Inc.,*** Tax Appeals Tribunal, August 11, 1988).

In ***Matter of Ilter Sener*** (***supra***), the Tax Appeals Tribunal stated, "[w]hen analyzing state

statutes modeled after federal statutes, we may look to federal cases for guidance." The Tribunal continued, "[t]he income tax late payment and fraud penalty provisions were modeled after similar federal statutes (see I.R.C. §§ 6651, 6653) . . . [and] [t]he sales tax penalty provisions were modeled after those in the income tax laws." Because the language of Tax Law §1145(a)(2) (the sales tax fraud penalty statute) is similar to that of Tax Law § 289-b(1)(d), and because section 289-b(1)(d) was enacted in 1985 (L 1985, ch 44) and after the enactment of section 1145(a)(2), I find that the petroleum business tax fraud penalty statute is modeled after the same federal statutes, and that reliance on federal case law for guidance is permissible.

F. In ***Frazier v. Commissioner*** (91 TC 1, 12) the U. S. Tax Court held, "fraud may be proved by circumstantial evidence since direct proof of the taxpayer's intent is rarely available . . . [and] . . . [t]he taxpayer's entire course of conduct can often be relied on to establish the requisite fraudulent intent." In ***Merritt v. Commissioner*** (301 F2d 484, 62-1 US Tax Cas ¶ 9408), the Fifth Circuit held that, "[t]he mere understatement of income, standing alone, is not enough to carry the burden [to prove fraud] . . . ." But, "consistent and substantial understatements of income is by itself strong evidence of fraud." In ***First Trust and Savings Bank v. United States*** (206 F2d 97, 53-2 US Tax Cas ¶ 9496), the Eighth Circuit Court of Appeals stated that, "the filing of false returns is affirmative fraudulent conduct which is adapted to bring about deficiency of tax and an intent to evade tax may be inferred from it." The Court cited to ***United States v. Croessant*** (178 F2d 96, 49-2 US Tax Cas ¶ 9483), and quoted, with approval, the following language,

> [T]he man who files a wilfully false return has endeavored to mislead his government. He creates the appearance of having complied with the law, whereas his neighbor who has filed no returns does no such thing. Not

> only has he created the appearance of complying but that apparent compliance stands a good chance of remaining unattacked, for the tax authorities cannot possibly audit every taxpayer's return every year.

G. Viewing the evidence found in the Stipulation of Facts and attached documents against the background of the foregoing principles, it is to be seen that petitioner, during the course of the nine tax quarters under review, filed a petroleum business tax return for each quarter wherein it uniformly reported that all of its kero-jet sales made in New York were made to registered aviation fuel businesses or distributors of kero-jet fuel only or governmental entities, and were, therefore, not subject to the petroleum business tax (***see***, Finding of Fact "5"). All diesel motor fuel sold, received or possessed in New York State is presumed to be subject to the petroleum business tax by operation of Tax Law §§ 285-b(2) and 315(b)(iii). Petitioner has failed to substantiate through the presentation of exempt transaction certificates or similar documents that the sales reported in its returns were, in fact, exempt from the tax. In furtherance of petitioner's claim that all of its kero-jet fuel sales are petroleum business tax exempt, it paid the minimum tax of $25.00 per month with each of its quarterly returns (Tax Law § 301-a[a]). Petitioner paid a total of $675.00 for the nine quarters of the audit period, when, in fact, it should have paid $842,228.60 as the petroleum business tax due on its kero-jet sales for the audit period of 5,844,662 gallons. Another reason that petitioner should have paid over to the Division the sum of $842,228.60 is that during the audit period petitioner collected $842,228.60 from its customers as and for petroleum business tax. Of this sum, petitioner paid only $675.00 to the Division, and retained the difference, $841,553.60, for its own purposes.

H. In support of its contention that fraud penalty should not be imposed petitioner references the annual audits conducted by Coopers and Lybrand which examined records at

petitioner's corporate headquarters pertaining to its compliance with state tax requirements and the fact that management was never advised by the auditors of any New York State Tax Law Article 13-A reporting deficiencies. The internal pricing sheets prepared by the on-site manager of the New York FBO showed that the petroleum business tax was included in the selling price of the kero-jet fuel it sold during the audit period. These sheets were submitted for approval to a corporate vice-president located in Houston, Texas, who then provided summaries of the total sales price and volume sold at the New York FBO to petitioner's accounting department at the corporate headquarters in Newtown, Pennsylvania. The internal pricing sheets were not sent to the Newtown headquarters. There could not have been full disclosure of all pertinent information to petitioner's public accountants if the only documents showing the inclusion of the petroleum business tax in the selling price at the New York FBO were withheld from the Newtown corporate headquarters where the public accounting firm conducted its annual audits. In ***Matter of Cinelli*** (Tax Appeals Tribunal, September 14, 1989), the petitioner failed in his effort to attribute the underreporting of sales tax to his accountant's negligence where it was determined that he supplied incomplete information to his accountant. In ***Korecky v. Commissioner*** (781 F2d 1566, 86-1 US Tax Cas ¶ 9232), the Eleventh Circuit held that the Tax Court's finding of fraud was supported, *inter alia*, by the fact that petitioner provided his bookkeeper with only a summary of his retail sales instead of actual register tapes, which practice served to prevent a full disclosure of retail sales to the bookkeeper. Here, key records reflecting the details of the New York FBO's pricing practices, which information was needed by petitioner's accounting department to prepare accurate petroleum business tax returns and by petitioner's public accountants to confirm the accuracy of those returns, was, as a matter of course throughout the

audit period, kept from the accounting department and the public accounting firm by petitioner's New York FBO on-site manager, and its Texas-based vice-president responsible for the oversight of that FBO. It is noteworthy that the record is not without evidence that serves to impute knowledge of the New York FBO pricing practices and the inclusion of the petroleum business tax in the selling price of the kero-jet fuel to corporate managers and officers. The statement of Mr. Sipe, the general manager, (see Finding of Fact 14) alone, of itself and in the form presented, does not rise to the level of clear and convincing evidence of fraudulent conduct, but it is accorded some weight.

I. At the onset of the audit the Division made a request for books and records that included a specific request for exemption and resale certificates. This request was repeated during the course of the audit. The records supplied by petitioner included copies of the petroleum business tax returns but no exemption or resale certificates, notwithstanding that petitioner reported that all of its kero-jet fuel sales were exempt from the petroleum business tax.

Proof of consistent and substantial understatements of income coupled with incomplete and inaccurate records, plus evidence that petitioner did not provide its accounting department with all the information necessary for filing complete and accurate petroleum business tax returns is sufficient to support a finding of fraud (***Merritt v. Commissioner, supra***). Fraud penalty is sustained.

J. The petitions of Aero Services International, Inc. are denied and the nine notices of determination are, in all respects, sustained.

DATED: Troy, New York
November 8, 2001

/s/ Gary R. Palmer
ADMINISTRATIVE LAW JUDGE