

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
MOHAMED IBN MOHAMED ASSANA : DETERMINATION
D/B/A UNITED DELI & GROCERY : DTA NO. 818063
:
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 March 1, 1995 through November 30, 1997. :

Petitioner, Mohamed Ibn Mohamed Assana, d/b/a United Deli & Grocery, c/o Tony Antonious, 6110 Alderton Street, #D3, Rego Park, New York 11374, 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 March 1, 1995 through November 30, 1997.

A hearing was held before Thomas C. Sacca, Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on June 11, 2001 at 10:30 A.M., with all briefs to be submitted by August 10, 2001, which date began the six-month period for the issuance of this determination. Petitioner appeared *pro se*. The Division of Taxation appeared by Barbara G. Billet, Esq. (Michael B. Infantino, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation's use of an observation test was reasonably calculated to reflect tax due.

II. Whether petitioner has established that reasonable cause exists so as to justify the waiver of penalties.

FINDINGS OF FACT

1. Mohamed Ibn Mohamed Assana (“petitioner”) operated a grocery store/deli known as the United Deli & Grocery at 812 10th Avenue, New York, New York at which beer, soda, cigarettes, sandwiches and certain food items were sold. The store was open 24 hours a day, 7 days a week.

2. In December 1997, the Division of Taxation (“Division”) commenced a field audit of petitioner’s business. The auditor visited the place of business and gave the manager his business card. On December 10, 1997, the auditor sent a letter to petitioner scheduling a field audit of petitioner’s books and records pertaining to sales and use tax liability for the period March 1, 1995 through November 30, 1997. The letter asked that the following records be made available for examination: financial statements; journals; ledgers; sales invoices; purchase invoices; cash register tapes; sales and use tax returns; Federal income tax returns; and exemption certificates.

At the scheduled meeting petitioner provided no books and records to the auditor.

3. Based on the lack of books and records, the auditor determined that a detailed audit would be impossible. Important to this determination was the fact that no source sales documents such as cash register tapes or sales invoices were provided and that there was no documentation of tax collected or of taxable sales. The auditor concluded that an observation test would be conducted to determine petitioner’s taxable sales for the audit period.

4. On April 8, 1998, a Wednesday, a 12-hour observation test was performed at the business premises of petitioner. During the hours of 7:00 A.M. through 1:00 P.M., two auditors placed themselves on each side of the cash register which was located at the front of the store. Two different auditors were in the same locations during the hours of 1:00 PM through 7:00

P.M. During the observation the auditors observed that petitioner did not charge or collect sales tax, but simply rang up the price of the goods sold for both taxable and nontaxable items. For the 12- hour period the auditors observed total sales of \$2,231.85, listing each item purchased and the amount paid. The auditor determined taxable and nontaxable sales, backed out the sales tax on taxable sales as if sales tax had been included in the price with the result that gross sales for the 12 hours of the observation equaled \$2,100.56. This figure was comprised of nontaxable sales of \$509.23 and taxable sales of \$1,591.33. Sales for the period 7:00 P.M. to 7:00 A.M. were estimated to be 50 percent of sales that had occurred during the earlier 12-hour period, based upon audit experience. For the 24-hour period, gross sales were computed to be \$3,150.00 and taxable sales \$2,387.00. The gross sales amount determined for the 24-hour period of \$3,150.00 was multiplied by 90 days to arrive at gross sales per quarter of \$283,500.00, which was multiplied by 11 quarters to arrive at gross sales for the audit period of \$3,118,500.00. The same computation was applied to the taxable sales for the 24-hour period of \$2,387.00 to arrive at taxable sales per quarter of \$214,830.00 and taxable sales for the audit period of \$2,363,130.00. Taxable sales for the audit period were multiplied by the tax rate of 8.25% to determine sales tax liability of \$194,958.23, and subtracting the sales tax reported for the audit period of \$1,761.00 resulted in sales tax due of \$193,197.23.

Penalties were imposed by the auditor for petitioner's failure to maintain books and records and failure to report and pay the tax due. An additional penalty was imposed as a result of the underreporting of tax due exceeding 25% of the amount of the taxes required to be shown on the returns for the audit period.

5. During the audit petitioner executed two consents extending the period of limitation for assessment of sales and use taxes under articles 28 and 29 of the Tax Law which collectively

extended to June 20, 1999 the date by which the Division could assess tax due for the period March 1, 1995 through November 30, 1998.

6. On December 21, 1998, a Notice of Determination was issued to petitioner in the amount of \$193,197.28, plus penalty of \$74,656.80 and interest of \$61,344.14, for a total amount due of \$329,198.22 for the audit period.

7. Petitioner established at the hearing that he had prepaid \$14,991.96 in sales tax during the audit period, reducing the amount of tax due to \$178,205.32, plus penalty and interest.

SUMMARY OF THE PARTIES' POSITIONS

8. Petitioner alleges as follows:

a. that as a result of the expansion of the store after the period at issue and before the observation test, sales observed were greater than during the period at issue;

b. that the hours between 7:00 A.M. and 3:00 P.M. were the heaviest in sales volume, and that the store remained open after 3:00 P.M. mainly for purposes of cleaning, inventory and food preparation;

c. that the 50% estimate of sales during the hours between 7:00 P.M. and 7:00 A.M. was too high and not verified;

d. that the listing of items purchased during the observation test by the auditors was not sufficiently detailed and mistakes were made in the amount column of items purchased.

9. The position of the Division may be summarized as follows:

a. Since petitioner failed to maintain adequate books and records, the Division was within its rights to employ external indices to determine petitioner's tax liability;

b. Petitioner has failed to prove that the audit methodology or the amount of the assessment was erroneous;

c. There is no basis to abate the penalties assessed as petitioner has failed to establish reasonable cause for his failure to report and pay the tax determined to be due.

CONCLUSIONS OF LAW

A. It is well established that every person required to collect tax must maintain and make available for audit upon request records sufficient to verify all transactions in a manner suitable to determine the correct amount of tax due (Tax Law § 1135[a]; 20 NYCRR 533.2[a]). Failure to maintain and make available such records, or the maintenance of inadequate records, will result in the Division's estimating tax due (Tax Law § 1138[a]; *see, Matter of Ristorante Puglia, Ltd. v. Chu*, 102 AD2d 348, 478 NYS2d 91, 93; *Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451, 452). To determine the adequacy of a 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. The purpose of such an examination is to determine whether 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 Adamides v. Chu*, 134 AD2d 776, 521 NYS2d 826, *lv denied* 71 NY2d 806, 530 NYS2d 109; *Matter of King Crab Rest. v. State Tax Commn.*, 134 AD2d 51, 522 NYS2d 978).

B. Petitioner received an audit appointment letter specifying the sales tax records requested for audit review. No cash register tapes, sales invoices or other source documents to substantiate sales were provided to the auditor. In fact, no books and records of any kind were provided. Given the clear, written request for records, and the lack of any response thereto by petitioner, it was entirely appropriate for the Division's auditor to conclude that conducting a detailed audit of petitioner's records to verify taxable sales and sales tax due would be

impossible. Accordingly, the auditor's decision to go forward with an indirect auditing methodology and estimate sales tax due on the basis of external indices is sustained.

C. Where, as here, the Division seeks to determine 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, supra; Matter of W.T. Grant Co. v. Joseph*, 2 NY2d 196, 159 NYS2d 150, 157, *cert denied* 355 US 869, 2 L Ed 2d 75).

However, 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, supra*).

Since petitioner had no purchase records and had no source documentation to substantiate taxable sales and sales tax collected, the auditor's decision to use an observation test was clearly reasonable (*Matter of Meskouris Bros. v. Chu, supra*). The auditor, in determining whether additional tax was due, performed an observation test over a 12-hour period and then projected 50% of the results over the remaining 12 hours of a 24-hour period. Gross and taxable sales for the 24-hour period were then projected over the entire audit period. The applicable tax rate (8.25 percent) was applied to the resulting taxable sales for the period at issue (\$2,363,130.00) to arrive at a tax liability (\$194,958.23) from which sales tax reported (\$1,761.00) was subtracted, arriving at sales tax due of \$193,197.23.

D. At the hearing, petitioner established that he had prepaid \$14,991.96 in sales tax during the audit period, reducing the amount of tax due to \$178,205.32, plus penalty and interest.

As no other documentation was presented by petitioner which established by clear and convincing evidence that the methodology used by the auditor was unreasonable or that the amount assessed was erroneous (*see, Matter of Meskouris Bros. v. Chu, supra; Matter of Surface Line Operators Fraternal Org. v. Tully, supra*), no further adjustments to the amount of tax assessed are warranted.

E. Section 1145(a)(1)(i) authorizes the imposition of penalty for the failure to file a return or pay over the sales and use taxes due within the time required. Section 1145(a)(1)(vi) of the Tax Law authorizes the imposition of penalty upon a taxpayer for its omission from the total amount of sales and use taxes required to be shown on a return an amount which is in excess of 25 percent of the amount of such taxes required to be shown on the return. The commissioner may abate all penalty, pursuant to section 1145(a)(1)(iii), when it is determined that such omission was due to reasonable cause and not due to willful neglect. Petitioner bears the burden of establishing that there was reasonable cause, and not willful neglect, for the failure to report and pay the taxes in question (*Matter of F & W Oldsmobile, Inc. v. State Tax Commn.*, 106 AD2d 792, 484 NYS2d 188; *Matter of East End Student Transportation Corp.*, Tax Appeals Tribunal, March 26, 1992). Here, the record is devoid of any facts which establish reasonable cause for petitioner's failure to pay the tax due. Thus, there is no basis to abate the penalty without such grounds.

In fact, the record establishes that petitioner was guilty of willful neglect in his reporting of sales and use taxes. The business failed to maintain adequate records for purposes of verifying taxable sales. Penalties cannot be waived where a taxpayer's failure to maintain accurate records resulted in underreporting of sales and use tax due (*Matter of Rosemellia*, Tax Appeals Tribunal, March 12, 1992; *Matter of Lima Florists*, Tax Appeals Tribunal,

December 15, 1988). A substantial discrepancy between the sales tax reported on the returns and the sales tax found to be due is sufficient to sustain the penalties assessed (*Matter of S.H.B. Supermarkets v. Chu*, 135 AD2d 1048, 522 NYS2d 985). During the instant audit period, petitioner reported taxable sales of \$23,712.00 and the Division on audit determined taxable sales to be \$2,363,130.00, a deficiency of \$2,339,418.00. Petitioner's failure to maintain accurate records and the large deficiency resulting from the current audit are evidence of willful neglect and dictate against waiver of the penalties herein.

F. The petition of Mohamed Ibn Mohamed Assana d/b/a/ United Deli & Grocery is granted to the extent indicated in Finding of Fact "7" and Conclusion of Law "D", but in all other respects is denied, and the notice of determination dated December 21, 1998, except as so modified, is sustained.

DATED: Troy, New York
January 10, 2002

/s/ Thomas C. Sacca
ADMINISTRATIVE LAW JUDGE