STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
JOSEPH H. GRAY	:	DETERMINATION DTA NO. 819116
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, 1997 through August 31, 1999.	:	

Petitioner, Joseph H. Gray, 12 Elaine Place, Plainview, New York 11803, 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, 1997 through August 31, 1999.

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on April 8, 2003 at 10:30 A.M., with all briefs to be submitted by August 4, 2003, which date began the six-month period for the issuance of this determination. Petitioner appeared *pro se.* The Division of Taxation appeared by Mark F. Volk, Esq. (Robert A. Maslyn, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation properly determined additional sales and use taxes due from Lynbrook Stationers, Inc. for the period March 1, 1997 through August 31, 1999.

II. Whether petitioner was liable for the tax due as a person required to collect sales and use taxes on behalf of Lynbrook Stationers, Inc. for the period in issue pursuant to Tax Law §§ 1131(1) and 1133(a).

FINDINGS OF FACT

1. On or about March 13, 2000, the Division of Taxation ("Division") began an audit of Lynbrook Stationers, Inc., an office supply business located in Lynbrook, New York, for the period March 1, 1997 through November 30, 1999 (the "audit period"). On that date an appointment letter was sent to the corporation requesting books and records pertaining to sales tax for the audit period.

2. After two meetings with the corporation's representative, Mr. David Rosenblum, the only records produced were incomplete bank records, canceled checks, some sales invoices and a schedule indicating other deposits. Although further requests for records were made, no other documentation was forthcoming. Specifically, the Division requested but was not provided with worksheets related to sales tax returns, the general ledger, sales journal, cash receipts journal, purchase journal, check disbursements journal, bank deposit slips, resale certificates or exempt organization certificates.

3. Given the incomplete information provided, the auditor decided that there was insufficient data to perform a detailed audit and the decision was made to acquire the corporation's bank records in order to analyze its deposits for the entire audit period to establish taxable sales. After this was accomplished, non-sale deposits and sales tax paid with returns filed were subtracted from the deposits to arrive at actual taxable sales of $1,601,390.50. In addition, after examining the incomplete invoices provided by the representative, it was determined that six percent of total sales were nontaxable. Therefore, it was agreed that six percent of the actual taxable sales were also exempt, leaving taxable sales determined on audit of $1,505,307.08 and additional tax due of $127,951.10.

4. Mr. Rosenblum consented to the Statement of Proposed Audit Change for Sales and Use Tax on February 16, 2001, agreeing that Lynbrook Stationers, Inc. was liable for additional sales and use taxes in the sum of $127,951.10 plus interest for the audit period. No such consent was executed by or on behalf of petitioner.

5. Petitioner executed a Consent Extending the Period of Limitation for Assessment on March 31, 2000, permitting the Division until June 20, 2001 to assess him personally for any sales and use taxes due from Lynbrook Stationers, Inc.

6. Petitioner was, at times, the vice-president, secretary and treasurer of Lynbrook Stationers, Inc., owned 50 percent of its stock, received compensation from the corporation and was a director during the audit period. Over the course of approximately 20 years, petitioner invested over five hundred thousand dollars in the business. He signed all[1] sales and use tax returns on behalf of the corporation during the audit period (with the exception of February 1999 only) and had the authority to sign and did sign checks on the corporation's operating account, including checks remitting sales tax to the Division. Petitioner shared the daily managerial duties with Mr. Steve Zanville, including the hiring and firing of employees. In addition, petitioner reviewed invoices on a daily basis and was in charge of overseeing accounts payable.

7. Petitioner's involvement with the corporation ended on or about October 8, 1999, when he ceased working for the corporation. In a letter, dated October 22, 1999, to petitioner from the corporation's president, Steve Zanville, petitioner was informed that Mr. Zanville intended to "dissolve our relationship as joint stockholders." Although Mr. Zanville did not explain how he intended to accomplish the dissolution, it was apparent that he understood petitioner was no

[1]All sales and use tax returns for the audit period, except the return for February 1999, were entered into the record.

longer with the corporation as of October 8, 1999, but that he would be responsible for any "debt of [sic] financial obligations" incurred prior to October 8th.

8. On August 24, 2000, the auditor met with the corporation's representative, petitioner and his wife to discuss the case and transcribe bank statements.

9. Based upon all the information the auditor collected, a notice of determination was issued to petitioner, dated April 5, 2001, as a person responsible for the sales and use taxes determined to be due from Lynbrook Stationers, Inc. The notice asserted additional tax due of $127,951.10 plus interest of $34,398.92 for the period March 1, 1997 through August 31, 1999.[2]

SUMMARY OF THE PARTIES' POSITIONS

10. Petitioner argues that the audit methodology was flawed because it underestimated the amount of tax-exempt sales made by the corporation during the audit period. Petitioner contends that sales to numerous vendors were for resale and other sales were to exempt organizations.

11. Petitioner believes that he should not be held responsible for the additional taxes determined to be due from the corporation because his business partner, and the only other shareholder, destroyed the books and records of the business after he departed, making it virtually impossible for him to defend himself in this matter.

12. The Division asserts that the audit methodology was reasonable given the insufficient records produced by the corporation to substantiate its sales. After a proper request, adequate books and records were not forthcoming and the auditor utilized bank records to estimate taxable sales and sales taxes due.

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[2]The period does not include the quarter September 1 through November 30, 1999 because petitioner had left the company on October 8, 1999.

13. The Division contends that petitioner was a person responsible for the collection and payment of sales taxes on behalf of the corporation based on his duties and involvement with the corporation on a daily basis during the audit period. The Division does not believe it matters that petitioner was not an active participant in the sales tax audit. The critical factor was that he was a person responsible for the sales tax during the period in issue, which the Division believes it has demonstrated.

14. Ultimately, the Division argues that petitioner has not carried his burden of showing either that the audit methodology was erroneous or that he was not responsible for the tax asserted.

CONCLUSIONS OF LAW

A. Petitioner is not bound by the consent to taxes executed by Mr. Rosenblum on behalf of the corporation on February 16, 2001. Mr. Rosenblum did not represent petitioner in this matter and had no authority to legally bind petitioner to the terms of the consent. (***Matter of Bleistein,*** Tax Appeals Tribunal, July 27, 1995.) The Division of Taxation's reliance on ***Matter of Sica Electrical and Maintenance Corp.,*** (Tax Appeals Tribunal, February 26, 1998), is misplaced. The Division argues that the signed consent established a rational basis for the assessment with respect to petitioner, notwithstanding that it was signed by the corporation's representative for the benefit of the corporation. This position is not consistent with the ***Bleistein*** case, which refused to hold a corporate officer liable for the taxes consented to by the corporation. Further, since petitioner was not privy to what transpired between the corporation's representative and the auditor, the argument that the audit methodology has been deemed "rational" vis-a-vis petitioner by the consent executed by the corporation is meritless.

B. Here, the Division must establish that its audit methodology was proper and reasonable. Tax Law § 1138(a)(1) provides, in part, that if a return required to be filed is incorrect or insufficient, the amount of tax due shall be determined based on such information as may be available including, if necessary, an estimation based on external indices. However, the Division may not utilize external indices unless it first determines that the taxpayer's books and records are inadequate for purposes of verifying sales and purchases subject to sales and use taxes (***Matter of Chartair, Inc. v. State Tax Commn.,*** 65 AD2d 44, 411 NYS2d 41). To determine the adequacy of a taxpayer's records the Division must first request (***Matter of Christ Cella, Inc. v. State Tax Commn.,*** 102 AD2d 352, 477 NYS2d 858) and thoroughly examine (***Matter of King Crab Rest. v. Chu,*** 134 AD2d 51, 522 NYS2d 978) the taxpayer's books and records for the entire period of the proposed assessment (***Matter of Adamides v. Chu,*** 134 AD2d 776, 521 NYS2d 826, ***lv denied*** 71 NY2d 806, 530 NYS2d 109). The request for records must be explicit and not "weak and casual" (***Matter of Christ Cella, Inc. v. State Tax Commn., supra***). The purpose of such examination is to determine whether the taxpayer's books and 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 Chartair, Inc. v. State Tax Commn., supra; Matter of Ronnie's Suburban Inn***, Tax Appeals Tribunal, May 11, 1989). When the books and records are not sufficient, the Division may resort to external indices to estimate tax.

C. The record in this matter indicated that the auditor made several written and oral requests for books and records for the period March 1, 1997 through November 30, 1999 and that very little was produced by the corporation or petitioner, who attended a meeting regarding the production of books and records between the corporation’s representative and the Division on August 24, 2000. Specifically, neither the corporation nor petitioner produced worksheets

related to the sales tax returns worksheets, the general ledger, a sales journal, a cash receipts journal, a purchase journal, a check disbursements journal, bank deposit slips, resale certificates or exempt organization certificates. Without adequate source documentation the auditor was justified in using the information available to estimate taxable sales. Corporation bank records for the entire audit period were analyzed to determine sales, and adjustments were made for non-sale deposits and sales tax remitted with returns. In addition, the auditor examined available invoices and determined that six percent represented nontaxable sales. This percentage was applied to total sales estimated from his analysis of bank deposits.

In ***Matter of The Humphrey House, Inc.,***(Tax Appeals Tribunal, July 31, 1997), the Tribunal stated:

> [T]he Division must select an audit method which is reasonably calculated to reflect the tax due (***Matter of Urban Liqs. v. State Tax Commn.,*** 90 AD2d 576, 456 NYS2d 138), but exactness in the outcome of the audit is not required (***Matter of Markowitz v. State Tax Commn.,*** 54 AD2d 1023, 388 NYS2d 176, ***affd*** 44 NY2d 684, 405 NYS2d 454). The Administrative Law Judge determined that the record contained sufficient evidence to establish a rational basis for the audit (***Matter of Grecian Sq. v. New York State Tax Commn.,*** 119 AD2d 948, 501 NYS2d 219), placing the burden on petitioner 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).

Given the failure to produce most of the records requested and the insufficiency of the few that were submitted, the Division was justified in resorting to an indirect methodology to determine petitioner's taxable sales and resulting tax liability.

D. Petitioner's argument that records did exist but were destroyed is rejected. Petitioner has not submitted any evidence to support this assertion other than to say that he reviewed certain books and records as part of his job duties and knew that they existed and were in good

order. In addition, his allegation that the records were destroyed after he left the business by his business partner and co-owner of the business, Mr. Zanville, was unsupported by the record.

Although petitioner contends that there were substantial sales to tax-exempt entities and sales made to vendors for resale which would result in fewer taxable sales, he was unable to supply proof of any such sales. Without more, petitioner's testimony was not sufficient to establish that the Division's estimated audit methodology was unreasonable (***Matter of Meskouris Bros. v. Chu, supra***).

E. 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]).

The resolution of whether a person is responsible to collect and remit sales tax for a corporation so that the person would have personal liability for the taxes not collected or paid depends on the facts of each case (***Matter of Cohen v. State Tax Commn.,*** 128 AD2d 1022, 513 NYS2d 564; ***Stacy v. State Tax Commn.,*** 82 Misc 2d 181, 183, 368 NYS2d 448). 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).

Based on the facts adduced in this matter there is no question that petitioner was a person responsible for the collection and payment of sales and use taxes by Lynbrook Stationers, Inc. He was a 50% stockholder, an officer and director of the corporation, signed all but one of the sales and use tax returns during the audit period, received compensation from the corporation, signed checks and had responsibility for the daily management of the business, including the hiring and firing of employees.

F. Petitioner's contention that he was "forcibly" and "legally" removed from the corporation by Mr. Zanville pursuant to the letter of October 22, 1999 was unfounded. That correspondence created more confusion than it resolved and was not the summary "removal from the business" that petitioner claimed. The letter merely notified petitioner of Mr. Zanville's intention to dissolve the relationship between the two men as "joint stockholders." The letter did not explain how Mr. Zanville, with an equal ownership percentage, would have been able to summarily discharge his equal partner and co-director. In reality, the letter appeared to be the first step in seeking to amicably dissolve the corporation.

Although Mr. Zanville emphasized petitioner's continuing liability for debts and obligations arising prior to his departure from the company on October 8, 1999, petitioner made no attempt to retrieve, copy or otherwise preserve records for his own protection, instead choosing to divorce himself completely from the business and expose himself to liability for the corporation's taxes. This behavior appears to have been inconsistent with petitioner's insistence that he believed his partner was misappropriating funds at that same time. Instead of taking proactive steps to protect himself and his substantial capital investment in the business, he

consciously chose to take no action. His inability to produce any records in support of his allegations was the direct result of his actions in October 1999 and thereafter and precludes this forum from granting his petition for relief. Quite simply, he has failed to sustain his burden of proof. (***See Matter of Leogrande v. Tax Appeals Tribunal***, 187 AD2d 768, 589 NYS2d 383, ***lv denied*** 81 NY2d 704, 595 NYS2d 398 [wherein the petitioner claimed that the Division had no basis for its estimations used in computing the notice, yet the petitioner submitted no evidence or testimony to sustain his burden of proof]; 20 NYCRR 3000.15[d][5].)

Petitioner argues that Mr. Zanville, by virtue of his alleged unilateral takeover of the business in October of 1999 and alleged destruction of the corporate books and records, should be solely liable for the taxes due from Lynbrook Stationers, Inc. These allegations have been determined to be unsupported by the record and are hereby rejected. Thus, petitioner is jointly liable for the taxes asserted due against the corporation. (***See, Matter of Jack Hurley*****,** Tax Appeals Tribunal, July 16, 1998 [wherein the Tribunal held that liability for taxes due is joint and several among responsible officers].)

G. The petition of Joseph H. Gray is denied and the Notice of Determination, dated April 5, 2001, is sustained.

DATED: Troy, New York
November 6, 2003

/s/ Joseph W. Pinto, Jr.
ADMINISTRATIVE LAW JUDGE