STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
BIANCULLI & SONS PRIVATE SANITATION, INC.	:	DETERMINATION DTA NO. 821312
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, 1999 through February 28, 2002.	:	

Petitioner, Bianculli & Sons Private Sanitation, Inc., filed a petition for revision of a determination or refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period March 1, 1999 through February 28, 2002.

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 June 26, 2007 at 10:30 A.M., with all briefs submitted by January 7, 2008, which date began the six-month period for the issuance of this determination. Petitioner appeared by Kestenbaum & Mark (Bernard S. Mark, Esq., of counsel). The Division of Taxation appeared by Daniel Smirlock, Esq. (Marvis A. Warren, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation properly determined additional tax due on sales, asset acquisitions and expense purchases for the audit period.

II. Whether the Division of Taxation properly asserted a penalty against petitioner for failing to pay the tax due and an additional penalty for omitting in excess of 25% of the tax which should have been reported on the return.

FINDINGS OF FACT

The Division of Taxation ("Division") submitted 35 proposed findings of fact pursuant to State Administrative Procedure Act § 307(1), all of which have been incorporated into the facts below, except findings 7, 13, 15 and 17, which did not accurately reflect the record; finding 14, which was argument; and findings 32, 33, 34 and 35, which are not relevant to this determination.

1. Petitioner, Bianculli & Sons Private Sanitation, Inc., was a sanitation business located at 4 O'Neil Avenue, Bayshore, New York, from March 1, 1999 through February 28, 2002 (the audit period), which provided garbage removal services and also removal services of materials brought to its three-acre transfer station facility located at the same address.

2. Petitioner operated the transfer station without required permits from the appropriate municipal government or the State of New York, and, therefore, did so illegally. On October 17, 2001, petitioner's president, Paul Bianculli, pled guilty to misdemeanor charges for maintaining the illegal transfer station.

3. The Division of Taxation performed a field audit of petitioner for the audit period which was begun by Ms. Jennifer Buscemi on March 18, 2002 and completed by Mr. David Fitzgerald in September 2005. The initial appointment letter and request for books and records was issued on March 29, 2002, with subsequent written requests made by letters of July 25, 2002, September 10, 2002, November 20, 2002, September 19, 2003, July 2, 2004, August 6, 2004 and January 24, 2006. Records requested included tax returns, the general ledger for the audit period, sales invoices for the audit period, exemption documentation, fixed asset purchase and sale invoices, expense purchase invoices, all bank statements, cancelled checks, deposit slips, cash receipts and disbursement journals and other relevant documentation.

4. The Division's review of petitioner's sales records indicated that they were inadequate because petitioner did not produce sales invoices or other original source documentation. Although it was found that gross sales were in agreement with the sales reported for federal income tax purposes, reconciliation with sales tax returns was impossible since petitioner did not report gross sales on its sales tax returns, only taxable sales.

5. The Division received information on two bank accounts maintained by petitioner during the audit period at European American Bank and the State Bank of Long Island. An analysis revealed that total deposits to the banks was $5,718,699.82,[1] which the Division determined was not in agreement with petitioner's books and records. From this figure, the Division subtracted those deposits attributable to town, county, exempt and U. S. Postal Service jobs. The remainder were identified as taxable sales or unexplained exempt sales. The Division totaled these sales for each month in the audit period, resulting in a difference between the taxable sales found by the Division and those reported by petitioner of $3,722,845.66.

6. The Division reduced the difference by the $6,376.00 of tax paid and subtracted sales to the State University at Stony Brook to arrive at audited taxable sales of $3,397,983.06. After subtracting reported sales of $77,280.00 the Division arrived at additional sales of $3,320,703.06 and additional tax of $275,607.21. This figure represented sales from the garbage route business and did not include sales made by petitioner at the illegal transfer station.

7. Sales at the transfer station were not documented by identifiable checks. The Division examined all checks deposited into the bank accounts for the month of June 2001and determined, in the absence of proof to the contrary, that they were received from regular garbage route

[1]This figure did not include a loan related to the State Bank of Long Island for April 2000 in the sum of $147,598.40, which was noted by Ms. Buscemi, but not included in the total deposits/sales column of her worksheet.

customers only. In addition, no invoices or sales receipts were produced which would have demonstrated that the checks were issued by customers other than regular garbage pickup customers.

8. Petitioner provided entries of yards of material collected from customers as recorded in a ledger. Petitioner informed the Division that it charged between $10.00 and $22.00 per yard for this service, but provided no breakdown of how much was charged at any discreet price. During the audit period, the transfer station received 116,891 yards of material, resulting in sales of $2,571,602.00 when multiplied by $22.00, and $213,352.01 in sales tax due.

9. The total additional tax on route and transfer station sales was determined to be $488,959.22.

10. After reviewing the asset acquisition records, the Division determined that the records were adequate and auditable, and revealed $128,123.50 in additional taxable asset purchases with resulting additional tax due of $10,570.19. Petitioner paid $9,893.94 of the additional tax on assets under the Division's amnesty program, leaving a remainder due of $676.25.

11. The Division also reviewed expense purchase records for truck expense, machinery repairs and maintenance and equipment rentals and found the records to be inadequate because approximately 80% of them were not found or produced. Those that were located and reviewed were filed in order by date. Petitioner never provided any invoices for machinery repair and maintenance and equipment rentals. Further, suppliers associated with these accounts could not be identified.

12. An analysis of truck expense invoices, the only expense invoices provided, revealed a tax error rate of .007763, which, when applied to total truck expense purchases of $230,867.77, resulted in an additional tax due of $1,792.22. Machinery repairs and maintenance purchases of

$35,123.66 and equipment rental purchases of $250,014.22 were all deemed taxable in the absence of any invoices and additional tax on these items was determined to be $2,925.12 and $20,626.17, respectively. Total additional tax due on all expense purchases was $25,343.51.

13. The total amount of additional sales and use tax due on sales, purchases and assets, less tax paid under amnesty on fixed assets, was determined on audit to be $514,978.98.

14. The Division issued a Notice of Determination to petitioner, dated August 25, 2005, which set forth additional tax due of $514,978.98, interest of $459,987.66 and penalty of $205,990.74, for a total due of $1,180,957.38.

15. Although the auditor, Mr. Fitzgerald, performed a test check of bank deposits for the month of June 2001, which included analyzing the names of customers, he was unable to discern if any were customers who paid petitioner for dumping at its transfer station since no invoices were presented to him to substantiate the claim that many were transfer station customers. Although petitioner submitted unsworn statements from seven individuals who stated they dumped at petitioner's transfer station, the Division did not attempt to contact the customers listed on checks deposited during June 2001, and petitioner did not have any other substantiating documentation relating any customers to transfer station sales during the audit period.

16. In operating its transfer station, petitioner collected the refuse and then transferred it, untreated, to other dumping stations for a fee. The fees petitioner paid to have the trash removed were acknowledged by the Division in its analysis of transfer station sales. Petitioner was able to profit in this business by charging customers one price for dumping small quantities at its transfer station and then paying at a volume discount for removal of the materials in larger quantities to other dumping stations. Most of the material received at the transfer station was construction debris.

17. After petitioner's transfer station was closed, a cleanup operation was commenced to return the property to an environmentally sound condition. During this operation, the building housing petitioner's business was subjected to severe water damage as a result of water used to contain dust. Petitioner had its books and records in boxes and admittedly did not take precautions to safeguard them during the cleanup. Even though a cleanup of the property where the books and records were stored was imminent, there was no plan to safeguard or transfer them to another location.

18. Petitioner relied on its accountants to prepare its tax returns and never made an independent decision, investigation or inquiry concerning the taxability of the transfer station sales.

19. In its brief, the Division conceded additional nontaxable sales which were discovered in the review of Mr. Fitzgerald's check deposit analysis for the month of June 2001. The 15 sales totaled $46,984.41 and resulted in a reduction of sales tax due of $3,894.32.

20. Ms. Toni Jean Bianculli worked for petitioner during the audit period. She was in charge of "managerial secretarial stuff" and did very little bookkeeping. Bookkeeping was done by another employee, Bob Rogers. Ms. Bianculli provided an undetermined number of invoices to the Division for expense purchases which were later destroyed.

CONCLUSIONS OF LAW

A. Tax Law § 1105(a) imposes a sales tax on the receipts from every "retail sale" of tangible personal property except as otherwise provided in Article 28 of the Tax Law. A "retail sale" is "[a] sale of tangible personal property to any person for any purpose, other than . . . for resale as such . . ." (Tax Law § 1101[b][4][i]). Tax Law § 1138(a)(1) provides, in relevant part, that if a sales tax return was not filed, "or if a return when filed is incorrect or insufficient, the amount of tax due shall be determined [by the Division of Taxation] from such information as may

be available. If necessary, the tax may be estimated on the basis of external indices . . . ." (Tax Law § 1138[a][1].) When acting pursuant to section 1138(a)(1), the Division is required to select a method of audit reasonably calculated to reflect the tax due. The burden then rests upon the taxpayer to demonstrate that the method of audit or the amount of the assessment was erroneous (***see Matter of Your Own Choice, Inc.,*** Tax Appeals Tribunal, February 20, 2003).

B. The standard for reviewing a sales tax audit where external indices were employed was set forth in ***Matter of Your Own Choice, Inc***., as follows:

> 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 purpose of the examination is to determine, through verification drawn independently from within these records (***Matter of Giordano v. State Tax Commn.***, 145 AD2d 726, 535 NYS2d 255; ***Matter of Urban Liqs. v. State Tax Commn.***, 90 AD2d 576, 456 NYS2d 138; ***Matter of Meyer v. State Tax Commn.***, 61 AD2d 223, 402 NYS2d 74, ***lv denied*** 44 NY2d 645, 406 NYS2d 1025; ***see also***, ***Matter of Hennekens v. State Tax Commn.***, 114 AD2d 599, 494 NYS2d 208), that they are, in fact, so insufficient that it is "virtually impossible [for the Division of Taxation] to verify taxable sales receipts and conduct a complete audit" (***Matter of Chartair, Inc. v. State Tax Commn.***, 65 AD2d 44, 411 NYS2d 41, 43; ***Matter of Christ Cella, Inc. v. State Tax Commn.***, ***supra***), "from which the exact amount of tax due can be determined" (***Matter of Mohawk Airlines v. Tully***, 75 AD2d 249, 429 NYS2d 759, 760).
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> Where the Division follows this procedure, thereby demonstrating that the records are incomplete or inaccurate, the Division may resort to external indices to estimate tax (***Matter of Urban Liqs. v. State Tax Commn.***, ***supra***). The estimate methodology utilized must be reasonably calculated to reflect taxes due (***Matter of W.T. Grant Co. v. Joseph***, 2 NY2d 196, 159 NYS2d 150, ***cert denied*** 355 US 869, 2 L Ed 2d 75), 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, ***affd*** 44 NY2d 684, 405 NYS2d 454; ***Matter of Cinelli***, Tax Appeals Tribunal, September 14, 1989). The taxpayer bears the burden of proving with clear and convincing evidence that the assessment is erroneous (***Matter of Scarpulla v. State Tax Commn.***, 120 AD2d 842, 502 NYS2d 113) or that the audit methodology is unreasonable (***Matter of Surface Line Operators Fraternal***

Org. v. Tully, 85 AD2d 858, 446 NYS2d 451; ***Matter of Cousins Serv. Station***, Tax Appeals Tribunal, August 11, 1988). In addition, "[c]onsiderable latitude is given an auditor's method of estimating sales under such circumstances as exist in [each] case" (***Matter of Grecian Sq. v. Tax Commn.***, 119 AD2d 948, 501 NYS2d 219, 221).

C. In this case, the record established the Division's clear and unequivocal written request for books and records of petitioner's sales, as well as petitioner's failure to produce such books and records. The auditor reasonably concluded that petitioner did not maintain or have available books and records that were sufficient to verify gross and taxable sales for the audit period.

The methodology utilized by the Division to determine sales was a bank deposit analysis which assumed all the deposits to petitioner's bank accounts were receipts from taxable sales, reducing said figure by taxes paid and demonstrated tax exempt sales to towns, counties, the United States Postal Service, the State University at Stony Brook and other tax exempt organizations. Since no evidence of sales at the transfer station was offered and an analysis of the checks for the month of June 2001 failed to identify any customers other than route customers, it was assumed that all deposits represented receipts from petitioner's route business.

As stated in Finding of Fact 19, the Division conceded that there were additional tax exempt sales which were identified among the checks tested by the auditor for the month of June 2001. As a result, the Division is directed to reduce the amount of additional sales tax due by $3,894.32.

D. There is no dispute that the rubbish removal service performed by petitioner is a taxable service. (Tax Law §1105[c][5]; 20 NYCRR 527.7[a][1].) Petitioner argues that because additional tax exempt sales were found in the June 2001 checks tested by the auditor, the Division should have credited petitioner for other tax exempt sales for the other months.

However, petitioner did not carry its burden of establishing with credible evidence that any additional tax exempt sales existed, even though invited by the Division on numerous occasions to do so. (***See Matter of Scarpulla***.)

Petitioner argues for concessions in the tax on additional sales based upon various errors it claims the Division committed. For instance, petitioner contends that tax exempt certificates were provided to the auditor at some point during the audit but were ignored. However, no copies supporting exempt sales not already credited by the Division were introduced at hearing, and no credible testimony was offered to demonstrate that exemption certificates were produced or reviewed by the Division on audit.

Petitioner also contends that the proceeds of a loan related to the State Bank of Long Island for the month of April 2000 in the sum of $147,598.40 was erroneously included in the deposits/sales column of the auditor's worksheet, resulting in additional audited sales. However, upon closer examination of the worksheet (Schedule B-1), it is apparent that this sum was noted but not included in the audited gross sales figure.

Petitioner challenges the results of the unexplained deposits because it claims the Division was informed that one of the bank accounts was dedicated to receipts from the transfer station only. However, except for unsworn statements from seven individuals who stated they dumped at petitioner's transfer station, petitioner submitted no other substantiating documentation which identified any customers as transfer station customers during the audit period, thus making it impossible to tell if any account represented transfer station customers alone.

Without adequate books and records to support its contentions, it is concluded that petitioner has failed to establish through credible documentary evidence or testimony that the Division's audit methodology was unreasonable and the assessment erroneous.

E. During a portion of the audit period, petitioner operated a transfer station where customers came with rubbish and debris (mostly construction debris), which was collected by petitioner and then disposed of without further treatment. Customers were charged for the service of dumping at the transfer station. The Division, acknowledging the operation and the receipts therefrom, utilized the number of cubic yards collected from general ledger data and multiplied that by $22.00,[2] a cost supplied by petitioner, to arrive at transfer station sales for the audit period.

Tax Law § 1105 (former [c][2]), in effect during the period in issue, provided that the receipts from every sale for the processing of tangible personal property were subject to tax. This was interpreted by the New York Court of Appeals in ***Matter of Cecos International, Inc. v. New York State Tax Commission*** (71 NY2d 934, 937, 528 NYS2d 811, 813 [1988]):

> With respect to invoices for services where the customer brought the industrial waste to the Cecos landfill and treatment facility, we agree with the Tax Commission that a nontaxable situation occurs only when the waste can be disposed of without further treatment. When treatment is required, a sales tax can be imposed pursuant to Tax Law §1105(c)(2), which allows a tax upon the receipts from the sale of the service of "processing. . . tangible personal property, performed for a person who directly or indirectly furnishes the tangible personal property * * * upon which services are performed" (Tax Law §1105[c][2]). Petitioner, referring to the four examples to the applicable tax regulation (20 NYCRR 527.4[d]), contends that the treatment does not constitute "processing" of personal property within the meaning of Tax Law §1105[c][2] because taxability requires that the tangible personal property be returned to the owner or someone

[2]Although $22.00 was the highest per yard charge petitioner supplied to the Division, it produced no evidence of discreet charges. Since the Division is not bound to exactness in its calculation of tax due in the absence of records, it is sufficient that it used a dollar amount utilized by petitioner. (***See Matter of Markowitz***.)

> within his dominion and control following processing. Neither the text of the statute nor the language of the regulation, however, so limits the definition of "processing". Inasmuch as petitioner treated the waste and the cost of treating it was passed on to the customer, "processing for the owner" resulted and the transaction was subject to taxation whether the property was returned to the customer or not. Here, the Commission's determination should be confirmed because the record indicates the Cecos charges its customers more for waste that must be processed than for waste that does not need processing.

The same rationale was cited in a Division Advisory Opinion, dated July 17, 1989, where the receipts from maintaining, servicing or repairing real property were deemed nontaxable when the trash removed from real property was brought to a site and then removed without further treatment. (Technical Services Bulletin, TSB-A-89[18]S.)

In this matter, it was established through Ms. Bianculli's credible testimony that petitioner merely accepted the debris and rubbish from customers and then hauled the trash (or had it hauled) to other sites without treating or processing the material at all. The profit was made on the volume discount, not on any value added due to processing the waste.

Since petitioner has established that these sales should have been found nontaxable by the Division, that portion of the assessment based upon the transfer station sales is canceled.

In an argument raised by the Division in a footnote to its brief, it mentioned that the Legislature added Tax Law § 1105(c)(5)(iv) which provided an exclusion from taxation for removal of waste material from a facility regulated as a transfer station. First, as indicated by the Division, this law did not take effect until three years after the audit period and is therefore irrelevant. Second, the exclusion covers the services of removing the waste material from the transfer station, not the service of accepting the debris at the station, which was the situation in this matter. Finally, the Division's conclusion that the new subsection would not apply to petitioner in any event because it was not regulated by the Department of Environmental

Conservation (DEC) is erroneous since the misdemeanor charges filed against Paul Bianculli were based on violations of DEC regulations and enforced by the New York State Environmental Conservation Police, which would indicate that the transfer station was at least arguably "regulated".

F. With respect to the additional tax determined to be due in the areas of asset purchases and expense purchases consisting of truck expense, machinery repair and maintenance, and equipment rentals, petitioner has only argued that Ms. Bianculli's testimony, which was not rebutted, proved that all taxes were paid on all rental items. This cannot be accepted based on the fact that petitioner produced records with regard to rental expense which were never established to be, or characterized by Ms. Bianculli as, all the records of rental expense purchases. In fact, it is doubtful she had the personal knowledge to draw such a conclusion. She testified that others had more administrative duties than she did, leaving to speculation whether she had undivided authority and access to pay and review rental expense invoices during the audit period. Indeed, she even stated that she did very little bookkeeping. Therefore, her own testimony cast significant doubt on her claim that petitioner always paid tax on the rental expenses. For these reasons, the Division's determination of additional tax due on asset and expense purchases is sustained.

G. Having concluded that the Division properly utilized an estimated audit methodology with respect to the route sales and that petitioner was unable to demonstrate that the results were erroneous, it must be determined if petitioner has established reasonable cause to abate the penalties imposed. The Division imposed penalty under Tax Law § 1145(a)(1)(i), which provides for penalty to be imposed where a person fails to pay over any tax within the time required by law, and Tax Law § 1145(a)(1)(vi), which provides that any person who omits from the total

amount of tax required to be shown on the return an amount in excess of 25% must pay a penalty of 10% of the amount of the omission. Tax Law § 1145(a)(1)(iii) and (vi) provide that the Division can remit the penalty if the failure to pay over the tax was due to reasonable cause and not willful neglect.

Petitioner argues that its loss of records in the hasty cleanup of the transfer station was through no fault of its own and constitutes reasonable cause for the underpayment of tax due.

In establishing reasonable cause for penalty abatement, the taxpayer faces an onerous task (***Matter of Philip Morris, Inc.***, Tax Appeals Tribunal, April 29, 1993). Referring to the mandatory language of Tax Law § 1145(a)(1)(i) , the Tribunal said that "the Legislature evidenced its intent that filing returns and paying tax according to a particular timetable be treated as a largely unavoidable obligation" (***Matter of MCI Telecommunications Corp.***, Tax Appeals Tribunal, January 16, 1992). In the instant matter, petitioner has not established that it maintained adequate records and certainly did not produce records as required. Petitioner's attempt to lay blame for its failure on the environmental cleanup is a red herring. It was well aware of the location of its records stored in boxes at its corporate headquarters and transfer station, yet it chose not to move them to a safe location and permitted a very destructive and sloppy cleanup operation to take place with the real possibility of losing the records. Petitioner's own gross negligence in caring for its records cannot form the foundation of reasonable cause to abate penalty. For these reasons penalties must be sustained.

However, given the cancellation of the tax determined to be due on the transfer station sales, the Division is directed to determine if petitioner remains liable for the penalty assessed pursuant to Tax Law § 1145(a)(1)(vi).

H. The petition of Bianculli & Sons Private Sanitation, Inc. is granted to the extent set forth in Conclusions of Law C, E and H above, but in all other respects is denied and the Notice of Determination, dated August 25, 2005, is sustained.

DATED: Troy, New York
July 3, 2008

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