

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

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In the Matter of the Petition :  
of :  
**KURT D. WILMARTH D/B/A ECHO TONE MUSIC** : DECISION  
for Revision of a Determination or for Refund of Sales and : DTA NO. 824936  
Use Taxes under Articles 28 and 29 of the Tax Law for the :  
Period December 1, 2006 through February 28, 2010. :

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Petitioner, Kurt D. Wilmarth d/b/a Echo Tone Music, filed an exception to the determination of the Administrative Law Judge issued on June 5, 2014. Petitioner appeared pro se. The Division of Taxation appeared by Amanda Hiller, Esq. (Robert A. Maslyn, of counsel).

Petitioner filed a letter brief in support of his exception. The Division of Taxation filed a letter brief in opposition, which also incorporated its brief previously submitted to the Administrative Law Judge. Petitioner filed a letter brief in reply on December 4, 2014. Petitioner's request for oral argument was denied. The six-month period for issuance of this decision began on December 4, 2014.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

***ISSUES***

I. Whether the indirect audit methodology utilized by the Division of Taxation was reasonable.

II. Whether petitioner has shown reasonable cause for abatement of penalties.

***FINDINGS OF FACT***

We find the facts as determined by the Administrative Law Judge except for findings of fact 2, 4, 9 and 10, which have been modified to more completely and accurately reflect the record. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

1. Petitioner, Kurt D. Wilmarth d/b/a Echo Tone Music, was a retail business making sales of small musical instruments and equipment. The store offered music lessons and repair services for most musical instruments and equipment. Located adjacent to the store were practice rooms that were rented on a monthly basis.

2. On October 27, 2010, Mr. Addam Effinger, the Division of Taxation's (Division) auditor, contacted petitioner by telephone. It was agreed during this telephone conversation that petitioner and the auditor would meet at petitioner's place of business on November 22, 2010 to begin the audit. Also on October 27, 2010, correspondence was sent to petitioner from the Division confirming that an audit of petitioner's sales and use tax records for the period September 1, 2006 through August 31, 2010 had been scheduled and that a meeting to begin the audit had been arranged for November 22, 2010 at petitioner's place of business. The correspondence informed petitioner that he must make available to the auditor his books and records for the entire audit period, including, but not limited to: (1) sales tax returns, worksheets, and canceled checks showing taxes paid; (2) a general ledger; (3) a general journal and closing entries; (4) sales invoices; (5) all exemption documents supporting non-taxable sales; (5) bank statements, canceled checks and deposit slips for all accounts; (6) a cash receipts journal, including sales journal, if applicable; and (7) a cash disbursements journal, including purchase

journal, if applicable. The correspondence also informed petitioner that he could be asked to provide additional information during the course of the audit. This initial correspondence was followed by numerous communications between the auditor and petitioner, regarding requests by petitioner to postpone the meeting date, corresponding requests from the auditor for waivers of the statute of limitations, and another provision to petitioner of the list of records he was required to produce at the meeting. The initial meeting was eventually held on January 18, 2011. At that time, petitioner provided: (1) tapes from his credit card machine for 2010 (with three register receipts mixed in); (2) sales sheets that were prepared by petitioner by adding his saved receipts together; and (3) some expense invoices for 2010. Concerned with petitioner's failure to provide any records, and statute of limitations issues, the Division obtained petitioner's bank statements through a third party subpoena, receiving the information on February 4, 2011. After further communications with petitioner, including additional requests for records, on April 21, 2011 the auditor and Ms. Donna VanAuken, the auditor's supervisor, met with petitioner at his place of business. At this second meeting, petitioner provided the Division with a book showing monthly room rental totals for 2009 and 2010 and some invoices from 2010 for his repair business.

3. After a review of the documents provided, the Division determined that petitioner's books and records were insufficient to conduct a detailed audit. The Division determined that the sales records were inadequate for the audit period since petitioner did not maintain any detailed invoices, guest checks or cash register tapes. The only records maintained were tapes from the credit card machine and a summary sales sheet for each year by month. The credit card tapes were incomplete since there were gaps in the numerical invoice numbers on the tapes provided.

Gross sales records were incomplete and could not be reconciled to any tax returns. The sales tax returns were reconciled to the federal income tax returns, which resulted in substantial differences in all years reviewed.

4. Having determined that petitioner's records were inadequate to conduct a detailed audit, the Division utilized a bank deposit analysis to calculate petitioner's sales. The auditor utilized the bank statements received from the third-party subpoena to determine petitioner's bank deposits over the course of the audit period. As detailed below, bank deposits attributable to practice/rehearsal room rental, music lessons and sales taxes paid were deducted from the total deposits because such receipts are not subject to sales tax.

5. The sales deemed for room rental were removed by the auditor based on petitioner's own unverifiable spreadsheets that he provided for all of 2009 through August 2010. Petitioner refused to provide the actual room rental contracts, yet the auditor accepted the unverifiable sheets and calculated an average of such sales per month of \$4,097.55, which amount was rounded up to \$4,100.00 per month and then projected over all of the quarters in the audit period.

6. The auditor was also faced with unverifiable amounts for music lesson sales, which the auditor also allowed as nontaxable, and credited petitioner with an average of \$2,400.00 per month. It is noted that both the credits given for room rentals and music lessons were not founded on any verifiable documentation despite the auditor's giving petitioner credit for these amounts.

7. Lastly, the auditor accepted, without verifiable documentation, that petitioner had deposited all collected sales tax into the bank. Thus, the auditor removed such amounts from the

bank deposits. This resulted in a determination of additional taxable sales of \$137,418.77 with sales tax due in the amount of \$10,993.50.

8. Statutory and omnibus penalties were imposed herein based upon the fact that the records produced for audit were inadequate; there was a substantial underreporting of sales tax due by more than 25%; and petitioner presented no evidence of any reasonable cause for his failure to properly report the sales tax due.

9. The Division issued notice of determination (L-036180064), dated June 2, 2011, to Kurt D. Wilmarth d/b/a Echo-Tone Music, asserting additional sales and use taxes due in the amount of \$10,933.50, plus penalties and interest. This notice was modified by a conciliation order issued on February 10, 2012, to a reduced tax liability of \$7,274.80 plus penalties and interest. This modification reflected an allowance for security deposits in connection with the rental of the practice/rehearsal rooms and an additional allowance for receipts from such rentals. Such modifications were based upon information provided by petitioner.

10. The parties agreed to have this matter determined on submission without a hearing. Petitioner did not submit any evidence or argument in support of his petition filed herein.

***THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE***

The Administrative Law Judge first explained that in order for the Division to resort to an estimated audit methodology, it must first request and examine a taxpayer's records to determine if such records are adequate to conduct a detailed audit. The Administrative Law Judge concluded that, in the present matter, petitioner failed to maintain and produce adequate records, thus enabling the Division to utilize an estimated audit methodology reasonably calculated to reflect petitioner's tax liability. The Administrative Law Judge noted that sales of and repairs to

musical instruments are taxable and that it was petitioner's burden to prove that either the Division's audit methodology or the amount of tax assessed was erroneous. The Administrative Law Judge ultimately concluded that petitioner had not met his burden as he had not introduced any evidence, or put forward any additional argument, in support of his petition.

***ARGUMENTS ON EXCEPTION***

Petitioner argues that during 2006 through 2008, his business was just starting and all of its receipts were from the rental of the practice/rehearsal rooms and the security and key deposits associated with those rentals. Furthermore, petitioner contends, that for the remainder of the audit period, taxable sales were minimal and the great majority of the business receipts were still from the rentals and fees associated with the rentals. Thus, petitioner argues that estimating his sales tax liability based upon a bank deposit analysis is grossly inaccurate and unfair.

The Division initially argues that the factual assertions made by petitioner in his notice of exception and letter brief should not be considered by this Tribunal as they are not part of the record in this matter. The Division then asserts that where, as here, the Division has resorted to an estimated audit methodology to determine the amount of tax asserted due, petitioner cannot prove that the amount of tax due asserted by the Division was erroneous or unreasonable simply by submitting his own estimate of tax due.

The Division asserts that its estimated methodology was reasonable in that its audit results are presumed to be correct in the absence of any credible evidence in the record challenging those results. The Division also asserts that a presumption of correctness attaches to a notice of deficiency issued by the Division, and it is petitioner's burden to overcome this presumption. As

petitioner in the present matter submitted no evidence, the Division argues that the notice should stand.

Furthermore, the Division argues that omnibus penalties for failure to report and pay sales tax in excess of 25% were properly imposed herein due to petitioner's failure to provide adequate books and records and his inability to substantiate his reporting of tax due. Finally, the Division asserts that the penalties should not be abated, as petitioner has not shown reasonable cause for these failures.

### ***OPINION***

Initially, we address the procedural issues raised by both the factual assertions set forth in petitioner's notice of exception and letter briefs, and petitioner's attempt to submit additional evidence with his letter brief in reply, which was rejected. With regard to the additional factual assertions made by petitioner on exception, for example, that nontaxable out-of-state sales were made during the audit period, we initially note that there is no evidence in the record to support such assertions. Furthermore, with regard to both petitioner's additional factual assertions and his attempt to submit new evidence on exception, "[w]e have held that a fair and efficient hearing process must be defined and final, and that the acceptance of evidence after the record is closed is not conducive to that end and does not provide an opportunity for the adversary to question the evidence on the record (*see Matter of Purvin*, Tax Appeals Tribunal, October 9, 1997; *see also Matter of Schoonover*, Tax Appeals Tribunal, August 15, 1991)" (*Matter of Ippolito*, Tax Appeals Tribunal, August 23, 2012, *confirmed sub nom Matter of Ippolito v Commissioner of N.Y. State Dept. of Taxation & Fin.*, 116 AD3d 1176 [2014]). We have applied the same rationale to assertions of additional facts on exception (*see Matter of Guffin*, Tax Appeals

Tribunal, September 18, 2014). Accordingly, we have not considered either the additional factual assertions made by petitioner on exception or the additional evidence petitioner attempted to submit with his reply brief.

Pursuant to Tax Law § 1132 (c) (1), petitioner bore the burden of proving by clear and convincing evidence that the tax assessed was erroneous (*Matter of Rizzo v Tax Appeals Trib. of State of N.Y.*, 210 AD2d 748 [1994]; *Matter of Mobley v Tax Appeals Trib. of State of N.Y.*, 177 AD2d 797, 799 [1991], *appeal dismissed* 79 NY2d 978 [1992]; *Matter of Surface Line Operators Fraternal Org. v Tully*, 85 AD2d 858 [1981]). Furthermore, a presumption of correctness attaches to a notice issued by the Division, and the taxpayer must overcome this presumption (*see Matter of Suburban Carting Corporation*, Tax Appeals Tribunal, May 7, 1998, citing *Matter of Tavalacci v State Tax Commn.*, 77 AD2d 759 [1980]; *Matter of Leogrande*, Tax Appeals Tribunal, July 18, 1991, *confirmed* 187 AD2d 768 [1992], *lv denied* 81 NY2d 704 [1993]).

There is no dispute that the audit methodology utilized in this matter was an indirect methodology not based solely on the books and records of petitioner. In order for the Division to utilize an indirect methodology, it must show that it made an adequate request for books and records for the audit period (*see Matter of Christ Cella, Inc. v State Tax Commn.*, 102 AD2d 352 [1984]), and that it reviewed the records provided in order to determine that the records were inadequate for the purposes of conducting a complete audit (*see Matter of King Crab Rest. v Chu*, 134 AD2d 51 [1987]).

The October 27, 2010, correspondence from the Division to petitioner constituted an adequate request for books and records and covered the entire audit period currently at issue.

This was followed by numerous other communications wherein records were requested. Pursuant to Tax Law § 1135 (a) (1), petitioner was required to keep records of every sale he made and the tax payable on each sale. However, the only records provided by petitioner in response to all of the Division's requests were: tapes from his credit card machine (with three cash register receipts mixed in) for 2010; sales sheets prepared by petitioner by adding his saved receipts together; some expense invoices for 2010; partial invoices for his repair business for 2010; and a book showing monthly room rental totals for 2009 and 2010 without any source documentation. Furthermore, at no time during these proceedings has petitioner even asserted that the Division did not make an adequate request for records. The field audit report reflects that the records provided to the Division were reviewed and determined to be inadequate. Based upon the record before us, it was acceptable for the Division to calculate petitioner's tax liability based on estimated or indirect audit methods.

While the Division may resort to an estimated or indirect audit method to calculate sales tax due where a taxpayer has failed to present books and records adequate for the Division to conduct a detailed audit (*see Matter of Urban Liqs. v State Tax Commn.*, 90 AD2d 576 [1982]), the method chosen by the Division must be reasonable (*see Matter of House of Audio of Lynbrook*, Tax Appeals Tribunal, January 2, 1992) and reasonably calculated to reflect the taxes due (*see Matter of W.T. Grant Co. v Joseph*, 2 NY2d 196 [1957], *cert denied* 355 US 869 [1957]; *Matter of Ristorante Puglia v Chu*, 102 AD2d 348 [1984]). The method need not be exact (*Matter of Markowitz v State Tax Commn.*, 54 AD2d 1023 [1976], *affd* 44 NY2d 684 [1978]) and the auditor is given considerable latitude in devising an audit method (*Matter of Grecian Sq. v New York State Tax Commn.*, 119 AD2d 948 [1986]).

Petitioner argues that the bank deposit analysis audit method utilized by the Division is grossly inaccurate and unfair, in that the great majority of the deposits at issue reflect nontaxable receipts from the rental of the practice/rehearsal rooms and associated fees. However, the auditor subtracted from petitioner's total bank deposits amounts estimated to be attributable to practice/rehearsal room rentals and music lessons, and the exact amount of sales taxes paid by petitioner during the period in issue, to arrive at petitioner's sales subject to tax. Indeed, the amounts subtracted for the room rentals and the music lessons were derived from amounts provided to the Division by petitioner. Furthermore, the amounts subtracted for sales taxes were the sales taxes actually paid by petitioner for the period at issue, even though petitioner provided no proof that such amounts were deposited into the bank account utilized by the Division in its analysis. Petitioner's assessed liability was further reduced as a result of a conciliation conference. This reduction was for amounts attributable to additional practice/rehearsal room rentals and security deposits associated with those rentals. The further reduction was again based upon information supplied by petitioner. Petitioner submitted no additional documentary evidence to the Administrative Law Judge. Thus, every piece of information provided by petitioner to the Division has already been incorporated into the Division's bank deposit analysis, first into the audit results and then into the conciliation order resulting from the conciliation conference. Based upon these facts, petitioner has failed to meet his burden of proof, showing that the Division's audit method was not reasonably calculated to reflect taxes due or that the amount of tax assessed was erroneous.

Finally, based upon petitioner's failure to introduce any evidence or argument for the abatement of penalties, we decline to address this issue.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Kurt D. Wilmarth d/b/a Echo Tone Music is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Kurt D. Wilmarth d/b/a Echo Tone Music is denied; and
4. The notice of determination dated June 2, 2011, as modified by the conciliation order,

dated February 10, 2012, is sustained.

DATED: Albany, New York  
June 4, 2015

/s/ Roberta Moseley Nero  
Roberta Moseley Nero  
President

/s/ Charles H. Nesbitt  
Charles H. Nesbitt  
Commissioner

/s/ James H. Tully, Jr.  
James H. Tully, Jr.  
Commissioner