

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
XIAO MING ZHU : DETERMINATION
 : DTA NO. 824417
for Revision of a Determination or for Refund of :
Tax on Cigarettes and Tobacco Products under :
Article 20 of the Tax Law for the Period Ended :
October 1, 2009. :

Petitioner, Xiao Ming Zhu, filed a petition for revision of a determination or for refund of tax on cigarettes and tobacco products under Article 20 of the Tax Law for the period ended October 1, 2009.

On February 26, 2013, petitioner, appearing by Xue & Associates, P.C. (Benjamin B. Xue, Esq., and Thomas H.C. Kung, Esq., of counsel), and the Division of Taxation, appearing by Amanda Hiller, Esq. (Michele W. Milavec, Esq., of counsel) waived a hearing and submitted this matter for determination based on documents and briefs to be submitted by July 12, 2013, which date commenced the six-month period for issuance of this determination. After review of the evidence and arguments submitted, Dennis M. Galliher, Administrative Law Judge, renders the following determination.

ISSUES

I. Whether the Division of Taxation properly determined that petitioner was a person who was in possession or had control of 280,044 counterfeit cigarette tax stamps so as to be liable for a penalty pursuant to Tax Law § 481(1)(b).

II. Whether, if so, the amount of the penalty imposed was excessive and constituted an abuse of discretion.

FINDINGS OF FACT

1. During the period 2003 through 2010, petitioner, Xiao Ming Zhu, operated Rong Cheng Fashion & Toys, a small clothing, shoe, souvenir, toy and local convenience store located at 4618A 8th Avenue, Brooklyn, New York.

2. On September 25, 2009, the New York City Office of Tax Enforcement (NYC OTE) received information from the United States Immigration and Customs Enforcement Service that a package from Hong Kong, China, containing counterfeit cigarette tax stamps had been intercepted at John F. Kennedy International Airport.

3. The package was shipped via DHL Express and was addressed for delivery to “Zhu Xiao Ming” at 4618A 8th Avenue, Brooklyn, New York. The package was from a “Mr. Hu”, and had been found to contain 280,044 counterfeit Commonwealth of Virginia cigarette tax stamps. Neither the delivery label nor the package itself identified its contents, other than bearing the description “sample of paper sheet.”

4. At approximately 5:55 P.M. on October 1, 2009, a NYC OTE investigator, posing as a uniformed DHL Express employee, executed a controlled delivery of the package from Hong Kong containing the counterfeit cigarette tax stamps to petitioner, Xiao Ming Zhu, at 4618A 8th Avenue, Brooklyn, New York. At the time of delivery, the package was tightly sealed by packing tape. The person who delivered the package did not inform petitioner of the contents of the package. Petitioner signed for and took physical possession of the package from Hong Kong.

5. Subsequent to the delivery of the package, a search warrant was executed at approximately 6:00 P.M. on October 1, 2009 at 4618A 8th Avenue, Brooklyn, New York, as part

of a joint operation by investigators from the New York State Department of Taxation and Finance—Office of Tax Enforcement--Petroleum, Alcohol, Tobacco Bureau (PATB) and the NYC OTE.

6. During the execution of the search warrant on October 1, 2009, the above-described package was located on the floor beside the service counter at the store. The package was confiscated, and was found to contain 280,044 counterfeit Commonwealth of Virginia cigarette tax stamps. Execution of the search warrant further resulted in confiscation of additional contraband found in or about the premises including 143.8 cartons of untaxed cigarettes, 1,000 sheets containing (in total) 108,000 counterfeit Commonwealth of Virginia cigarette tax stamps, and 9 sheets containing 972 counterfeit Commonwealth of Virginia cigarette tax stamps. At approximately 7:30 P.M., petitioner was arrested on the scene and was charged with the following:

- a) Criminal Possession of a Forged Instrument in the First Degree (Penal Law § 170.30);
- b) Attempt to Evade or Defeat Cigarette tax (Tax Law § 1814[a][1]);
- c) Transport for Sale of Untaxed Cigarettes (Tax Law § 1814[b]);
- d) Possession of Ten Thousand or More Untaxed Cigarettes (Tax Law § 1814[c][1]);
- e) Possession of Counterfeit Tax Stamps (Tax Law § 1814[g]);
- f) Attempt to Evade or Defeat Cigarette Tax (NYC Administrative Code § 11-4012[a][1]);
- g.) Possession For Sale of Untaxed Cigarettes (NYC Administrative Code § 11-4012[b]).

7. For reasons not specified in the record herein, the office of the Kings County District Attorney declined to prosecute the charges and the criminal case was closed. However, PATB

referred the matter to the Audit Division (Division) for assessment of a civil penalty based on petitioner's possession or control of 280,044 counterfeit cigarette tax stamps in violation of Tax Law § 481(1)(b).

8. On March 22, 2010, the Division issued to petitioner a Notice of Determination (L-033435160) assessing a penalty in the amount of \$5,600,880.00 for possession of unaffixed, altered, or counterfeit cigarette tax stamps in violation of Article 20 of the New York State Tax Law. The notice sets forth the "tax period ended" date of October 1, 2009, which was the date on which petitioner took possession and control of the package containing the counterfeit cigarette tax stamps and was arrested in connection with the DHL Express controlled delivery and subsequent execution of the search warrant as described in Findings of Fact 4, 5 and 6. Specifically, the notice states: "On 10/01/09, you were found to be in possession of unaffixed, altered, or counterfeit cigarette tax stamps, imprints or, [sic] impressions. Therefore, penalty is imposed under article 20 of the New York State Tax Law."

9. The penalty assessed by the Division pursuant to Tax Law, article 20, § 481(1)(b) was imposed at the rate of \$200.00 for every 10 unaffixed false, altered, or counterfeit cigarette tax stamps. By affidavit filed in this matter, the Division specifically stated the following:

Tax Law § 481(1)(b)(ii)(A)(III)(2) provides for a penalty of up to \$200.00 for every 10 unaffixed false, altered, or counterfeit cigarette tax stamps when quantities of more than 1,000 are knowingly in the possession or control of any person. In this case to calculate the penalty, the Division divided the total number of counterfeit tax stamps by 10 then multiplied that number by \$200.00. The following computation was used:

$$\begin{array}{r} 280,044 \text{ counterfeit tax stamps} \\ \div 10 \\ \hline 28,004.40 \\ \times \$200.00 \\ \hline \underline{\underline{\$5,600,880.00 \text{ penalty}}} \end{array}$$

10. Petitioner submitted an affidavit stating that his business (Rong Cheng Fashion & Toys) is located in a large and thriving new Chinese immigrant community. Petitioner stated that his neighbors and others in the community often use his business as a mail drop, with packages delivered there for later pick up. Petitioner avers that this practice assists members of the community by providing a safe place for delivery of packages to be retrieved later by those who are transient or migrant workers based in Brooklyn but working elsewhere. In his affidavit, petitioner states the foregoing practice, where he accepts packages addressed to him at his business location that he did not order and without knowledge of their contents, is a common occurrence. Petitioner, by his affidavit, states that he did not purchase, request or order the counterfeit cigarette tax stamps or cause the same to be shipped to him, and he further disavows any knowledge of a “Mr. Hu” from Hong Kong, China, and of the contents of the confiscated package at issue herein.

11. Petitioner does not dispute that the cigarette tax stamps in question were counterfeit tax stamps and were in his possession. On this score, the Division’s evidence details how petitioner signed for and accepted delivery of the package addressed to him in which the stamps were contained. Further, the Division’s agents who effected the delivery and subsequent arrest were trained in identifying counterfeit cigarette tax stamps, identified those at issue herein as counterfeit, and confirmed this conclusion by submitting the subject stamps for confirmatory testing conducted by the sole authorized producer of cigarette tax stamps for the Commonwealth of Virginia and for New York State and New York City during the period in question (Meyercord Revenue, Inc).

12. Petitioner submitted with his brief ten numbered proposed findings of fact and conclusions of law.¹ The Division submitted as part of its brief 14 numbered proposed findings of fact. In accordance with State Administrative Procedure Act (SAPA) § 307(1) the following rulings with respect to such proposed findings of fact are made:

Petitioner's proposed findings of fact numbered 2, 3, 4, 5, 7 and 9 have been accepted as supported by the record and are incorporated into the Findings of Fact set forth above.

Petitioner's proposed findings of fact numbered 1 and 10 are each rejected as setting forth an ultimate finding of fact thus constituting a conclusion of law.

Petitioner's proposed findings of fact numbered 6 and 8 are each rejected as not supported by the record and, additionally, proposed finding of fact 8 is rejected as setting forth an ultimate finding of fact thus constituting a conclusion of law.²

The Division's proposed findings of fact numbered 1 through 12 have been accepted as supported by the record and are incorporated into the Findings of Fact set forth above. Proposed findings of fact numbered 13 and 14 have not been incorporated because they set forth undisputed procedural matters whose recitation is unnecessary for purposes of resolving the issues presented.

SAPA does not require rulings with respect to proposed conclusions of law and none have been made herein.

¹ Petitioner's submission did not differentiate in any particular manner between proposed findings of fact and proposed conclusions of law.

² With respect to petitioner's proposed finding of fact 8, the record does not specify precisely at what point in time or by whom the delivered package was opened. However, since the delivery occurred at approximately 5:55 P.M., the search warrant was executed thereafter at approximately 6:00 P.M. (during which the contraband, including specifically the 280,044 counterfeit cigarette tax stamps, was discovered and recovered), and petitioner was not arrested until approximately 7:30 P.M. (i.e., after execution of the search warrant), it is reasonable to conclude that the package was opened during the execution of the search warrant and before petitioner was arrested.

CONCLUSIONS OF LAW

A. Tax Law § 481, Penalties and Interest, provides for the imposition of penalties and interest for violations of Tax Law Article 20, Tax on Cigarettes and Tobacco Products. The penalty provisions of Tax Law § 481(1)(b) include two subparagraphs, (i) and (ii). Both of these subparagraphs allow for the imposition of a penalty of up to \$200.00 for each ten unaffixed false, altered or counterfeit cigarette tax stamps, imprints or impressions (Tax Law § 481[1][b][i][B]; [ii][A][III][2]). Specifically, Tax Law § 481(1)(b)(i)(B) provides:

In addition to any other penalty imposed by this article, the commissioner may (B) impose a penalty of not more than two hundred dollars for each ten unaffixed false, altered or counterfeit cigarette tax stamps, imprints or impressions, or fraction thereof, in the possession or under the control of any person.

In contrast, Tax Law § 481(1)(b)(ii)(A)(III)(2) provides:

The penalties imposed by this subparagraph may be imposed by the commissioner in addition to any other penalty imposed by this article, *but in lieu of* the penalties imposed by subparagraph (i) of this paragraph:

not less than one hundred dollars but not more than two hundred dollars for each ten unaffixed false, altered or counterfeit cigarette tax stamps, imprints or impressions, or fraction thereof, in excess of one thousand unaffixed false, altered or counterfeit cigarette tax stamps, imprints or impressions, knowingly in the possession or knowingly under the control of any person. (emphasis added).

B. Carefully comparing the foregoing provisions reveals that the maximum penalty is the same under each, to wit, \$200.00 per ten counterfeit cigarette tax stamps.³ Likewise, each of the two provisions requires the counterfeit cigarette tax stamps to be “in the possession or under the control of” the person against whom the penalty is assessed. The penalties may not be imposed together, but rather the section 481(1)(b)(ii)(A)(III)(2) penalty may be imposed “in lieu of” the

³ For convenience and simplicity, the phrase “unaffixed false, altered or counterfeit cigarette tax stamps, imprints or impressions” shall be shortened herein to “counterfeit cigarette tax stamps.”

section 481(1)(b)(i)(B) penalty. The penalties differ in that the penalty under section 481(1)(b)(ii)(A)(III)(2) includes the additional requirements that a) the quantity of counterfeit cigarette tax stamps involved must exceed 1,000 such stamps and b) such counterfeit cigarette tax stamps must be *knowingly* in the possession or control of the person being penalized. Further, while there is no “low end” limit to the dollar amount of the penalty under section 481(1)(b)(i)(B), the penalty under section 481(1)(b)(ii)(A)(III)(2) specifies a “low end” limit whereby the penalty imposed may not be *less than* \$100.00 for each 10 counterfeit cigarette tax stamps in excess of 1,000 such stamps. Thus, while the Division’s discretion as to the penalty amount ranges from \$0.00 to \$200.00 under the first penalty provision, such discretion is limited in range from \$100.00 to \$200.00 under the latter provision. Accordingly, in instances involving larger amounts of counterfeit cigarette tax stamps, the Division’s penalty imposition must be at least for a minimum of \$100.00 per ten such stamps. It would appear that establishing such a required minimum penalty amount reflects the aim of assuring that those who engage in conduct involving counterfeit cigarette tax stamps on a larger level will be more severely penalized (at a minimum) than those operating on a smaller scale. At the same time, the imposition of this higher requisite minimum penalty carries with it the knowledge requirement set forth in the statute (i.e., “*knowingly* in the possession or *knowingly* under the control of . . .”). As detailed hereinafter, petitioner is properly subject to penalty under either Tax Law § 481(1)(b)(i)(B) or § 481(1)(b)(ii)(A)(III)(2).

C. As the Division points out, in this case the maximum penalty of \$200.00 per ten counterfeit cigarette tax stamps or fraction thereof was imposed. No lesser penalty amounts (i.e., less than \$200.00 per 10 stamps as allowed under the respective provisions described earlier) were computed. Thus the calculation of the maximum penalty under either of the two penalty

provisions results in the same penalty amount, and the Division asserts that the penalty was clearly imposed under Tax Law § 481(1)(b)(i)(B) at the maximum allowable rate specified therein. In support, the Division points out that the Notice of Determination simply states that petitioner was in possession of the counterfeit cigarette tax stamps in question in violation of Article 20 (*see* Finding of Fact 8), and since the notice does not on its face specify any quantity of counterfeit cigarette tax stamps or any knowledge requirement, per Tax Law § 481(1)(b)(ii)(A)(III)(2), then none was involved. In turn, petitioner does not dispute that the cigarette tax stamps in question were counterfeit or that he signed for and received into his possession and control the package containing such counterfeit cigarette tax stamps (*see* Finding of Fact 11). Without more, these circumstances fall within the penalty language of Tax Law § 481(1)(b)(i)(B), and the penalty is properly sustained thereunder.

D. However, in this case it is necessary to consider whether the penalty may also be sustained if the same was imposed under Tax Law § 481(1)(b)(ii)(A)(III)(2) rather than under Tax Law § 481(1)(b)(i)(B). This consideration becomes necessary because of the language in the Division's affidavit clearly specifying that the penalty was calculated pursuant to Tax Law § 481(1)(b)(ii)(A)(III)(2) (*see* Finding of Fact 9). The Division's affiant states that the penalty was "*calculated*" as opposed to "*imposed*" under Tax Law § 481(1)(b)(ii)(A)(III)(2). Nonetheless, since in this case the calculation of the amount of penalty is the same under either statutory provision, and since the language of the affidavit notes both the quantity and knowledge requirements of Tax Law § 481(1)(b)(ii)(A)(III)(2), the question of which provision the penalty was *imposed* under remains open.⁴ Since the penalty under Tax Law § 481(1)(b)(ii)(A)(III)(2)

⁴ As to calculation of the penalty, the Division did not choose to allow or impose any of the lesser possible penalty amounts resulting from the calculation options available under the separate penalty provisions, from which it might have been possible to ascertain which of the two provisions applied. Instead, the calculation simply involved

may only be imposed in lieu of, but not together with or in addition to, the penalty under section 481(1)(b)(i)(B), the foregoing ambiguity at a minimum compels the need to address whether the penalty is sustainable under Tax Law § 481(1)(b)(ii)(A)(III)(2) with its accompanying additional requirement that there must be “knowing” possession or control of the counterfeit cigarette tax stamps.

E. The penalty provision set forth in Tax Law § 481(1)(b)(ii)(A)(III)(2) requires physical possession or control plus knowledge that the possessed contraband was counterfeit cigarette tax stamps. Generally, possession is sufficient to permit an inculpatory inference that the possessor knows the nature of that which he possesses (*People v. Reisman*, 29 NY2d 278 [1971], *cert denied* 405 US 1041 [1972]). Notwithstanding that the package may not have been physically opened by petitioner, knowledge of the contents of a package addressed, delivered to, and in the possession of a specific addressee such as petitioner may be shown circumstantially by the surrounding conduct, events and circumstances of the possession (*Id.*). In *Reisman*, the Court of Appeals sustained a criminal conviction for possession of a dangerous drug based upon the circumstances of the defendant’s attempt to claim two cartons containing the drug at John F. Kennedy Airport. The Court explained that

Knowledge, of course, may be shown circumstantially by conduct or directly by admission, or indirectly by contradictory statements from which guilt may be inferred. * * * Generally, possession suffices to permit the inference that the possessor knows what he possesses, especially, but not exclusively, if it is in his hands, on his person, in his vehicle, or on his premises. * * * This, of course, is an elemental inference based on common experience and all but universal probabilities. Thus it is an ancient rule of inference or rebuttable presumption of fact that the recent and exclusive possession of the fruits of any crime warrants the inference of guilt,

applying the maximum allowable penalty amount (\$200.00 per ten counterfeit cigarette tax stamps) to the number of counterfeit stamps involved, with the dollar result being the same under either of the penalty provisions.

including, when material, knowledgeable possession” (*id.*; citations omitted).

An inference or rebuttable presumption of knowledgeable possession is not something that can be assessed in the abstract, but depends upon the particular circumstances in which the inference is to be drawn (*id.*; *see People v. Accosta*, 174 AD2d 181 [1992]). Thus, the inference of knowledge from the fact of possession rests on nothing more than the common and frequently justified perception that those who come into the possession of contraband most probably know the nature of what they possess (*People v. Accosta*). Where there are circumstances which make it less probable that the possession is knowing, the inference or presumption of fact may be rebutted (*Id.*).

F. The evidence in this case, taken as a whole, amply supports the conclusion that petitioner knowingly accepted possession and control of the counterfeit cigarette tax stamps. Notwithstanding petitioner’s general statements of explanation and denial, by affidavit, that his business was used as a “mail drop,” that he often accepted packages for others, and that he did not know the contents of the package in question and did not know a Mr. Hu (the listed sender) in China, it remains that the package containing the counterfeit cigarette tax stamps was addressed directly to petitioner and petitioner signed for and accepted the same. The assertions concerning petitioner’s location being used as a mail drop are unsupported by any direct evidence of instances where this occurred. Such a claim that petitioner was a mere unknowing holder might be more tenable if the package had not been addressed solely to petitioner but rather had been addressed to another person (e.g., addressed to its alleged recipient “in care of” petitioner). At a minimum, the question of how the alleged actual intended recipient might be identified to petitioner’s satisfaction so as to support his release of the “held” package to such person is not

addressed in petitioner's affidavit and remains unanswered. While petitioner might be reticent to identify the alleged "true" owner, an explanation of the process by which the alleged owner would claim a package addressed directly to petitioner, might lend some credence to the claim that petitioner did not know what was in the package and that he was somehow an unwitting "dupe" recipient thereof. As noted, petitioner submitted an affidavit but did not appear at a hearing to offer testimony, thus precluding any opportunity for cross examination including, presumably, questions concerning who the package was intended for, if not petitioner, and how petitioner would know into whose custody the package should be released. There is no question that competent evidence can be submitted by affidavit, as authorized by the Tribunal's regulations (20 NYCRR 3000.15[d]), and findings of fact may be made on the basis of affidavits (*see Matter of Orvis Co. v. Tax Appeals Tribunal*, 86 NY2d 165 [1995], *cert denied* 516 US 989 [1995]). However, statements made by affidavit are not subject to cross examination thus precluding the opportunity for the trier of fact to observe the demeanor of the witness and assess the credibility of the statements made. This lack of opportunity for cross examination and observation of demeanor, including the inability to delve into matters not addressed in petitioner's affidavit, leaves relevant questions unanswered and weighs against petitioner's position.

G. Further support for an inference of knowledge of the contents of the package may be taken from the discovery of like-contraband at the scene at the time of the delivery of the subject package and execution of the search warrant, including cartons of unstamped cigarettes as well as a significant number of additional counterfeit Commonwealth of Virginia cigarette tax stamps (*see* Finding of Fact 6). The presence of such contraband items makes it reasonable to accept that petitioner was engaged in selling cigarettes bearing counterfeit cigarette tax stamps or selling

the counterfeit cigarette tax stamps themselves. Further, the manner in which traffic in contraband such as counterfeit cigarette tax stamps is conducted together with the undeniably significant monetary value of such counterfeit stamps makes it unlikely that someone would mail the same addressed as they were to a random mail drop unless the intended recipient was petitioner, the addressee. Ultimately, the burden of establishing by clear and convincing evidence that the Division's determination imposing the penalty at issue was erroneous rests upon petitioner (*Matter of Leogrande v. Tax Appeals Tribunal*, 187 AD2d 768 [1992], *lv denied* 81 NY2d 704 [1993]).⁵ In this case, there is nothing in the record beyond petitioner's bare affidavit in support of his general denial of knowledge of the contents of the package in his possession. Thus, petitioner has failed to rebut the permissible inference of such knowledge and a penalty imposed pursuant to Tax Law § 481(1)(b)(ii)(A)(III)(2) is properly sustained.

H. Finally, petitioner has argued that the Division's imposition of the maximum allowable penalty was harsh, improper and an abuse of discretion given the mitigating factor that petitioner has never before been charged with any Tax Law violations, including any cigarette tax violations. The discretion to impose a penalty in an amount that is less than the maximum penalty amount is limited only insofar as the noted \$100.00 per ten counterfeit stamps "low end" limit in cases (such as this one) involving more than 1,000 counterfeit stamps (*see* Conclusion of Law B). Otherwise, the imposition of penalty and the calculation of the amount thereof rests squarely within the discretion of the Division (*Matter of Vinter*, Tax Appeals Tribunal, September 27, 2001), and "[i]t is not necessary for the Division to have considered any

⁵ It is noteworthy that it is permissible to draw an inference (or rebuttable presumption) of knowledge based on possession, as above, in criminal matters where the attendant standard of proof (beyond a reasonable doubt) is significantly higher than that applicable in matters involving the propriety of an assessment of a tax or an attendant penalty (clear and convincing evidence).

mitigating factors prior to the imposition of the penalty [under Tax Law § 481(1)(b)] since this is neither mandated by statute nor regulation” (*Matter of Fakhouri*, Tax Appeals Tribunal, July 5, 2007). Consequently, while the Division may exercise discretion as to the dollar amount of the penalty it imposes, the same is not mandated. The Division may (as it did) impose the maximum allowable penalty, and that result is not a matter within the purview of review or adjustment in this forum (*Id.*).

I. The petition of Xiao Ming Zhu. is hereby denied and the Notice of Determination dated March 22, 2010 is sustained.

DATED: Albany, New York
December 19, 2013

/s/ Dennis M. Galliher
ADMINISTRATIVE LAW JUDGE