STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions	:	
of	:	
PRIMA ASPHALT CONCRETE, INC.	:	DETERMINATION DTA NOS. 826279
for Revision of a Determination and for Refund of Sales and Use Taxes under Articles 28 & 29 of the Tax Law for the Period September 1, 2006 through February 28, 2010.	:	AND 826280

Petitioner, Prima Asphalt Concrete, Inc., filed petitions for revision of a determination and for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 2006 through February 28, 2010.[1]

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, in New York, New York, on May 15, 2015 at 10:30 A.M., with all briefs to be submitted by September 22, 2015, which date began the six-month period for the issuance of this determination. Petitioner appeared by Sales Tax Defense LLC (Mark L. Stone, CPA, and Jennifer L. Koo, Esq., of counsel). The Division of Taxation appeared by Amanda Hiller, Esq. (Nicholas A. Behuniak, Esq., of counsel).

ISSUES

I. Whether petitioner may reduce the sales tax due on prior sales to account for a volume discount subsequently provided to customers on said sales.

II. Whether a debit to the sales tax payable account to neutralize an opening credit balance was properly disallowed by the Division of Taxation.

[1]The petition filed under DTA No. 826279, with regard to the denial of petitioner's refund claim has been resolved. This determination will address only the issues related to the petition filed under DTA No. 826280.

FINDINGS OF FACT

The Division of Taxation (Division) submitted five proposed findings of fact, which have been incorporated into the facts below, except proposed finding of fact 2, where reference to sales to related parties was omitted as irrelevant.

1. During the period September 1, 2006 through February 28, 2010 (audit period), petitioner Prima Asphalt Concrete, Inc., was a manufacturer of asphalt and asphalt-related products that sold its products to contractors directly. Ronald Fehr, the president of petitioner during the audit period, explained that the sale of asphalt comprised about 90 percent of the company's sales.

2. Customers' trucks came to petitioner's business location where they were loaded with asphalt pursuant to payment agreements reached between petitioner and the customers, usually oral and in accordance with posted prices. Once trucks were loaded, the asphalt was transferred to the customers for transportation to and use at destinations determined by the customers. Product was purchased and picked up when it was to be used, and customers were billed on the 15th and 30th of every month for product that had been purchased during that time period.

3. Petitioner posted prices for the asphalt but often offered discounts to customers as an incentive to gain and retain customers. Due to competition in the marketplace, and to prevent the customer from shopping for lower prices or switching to another asphalt supplier before its order was completely filled, petitioner offered volume discounts that were applied to a customer's purchases after it met the volume goal, usually when the entire order had been filled. Since large orders could be filled over the course of one or more years, monthly invoices for purchases would show sales prices and tax thereon that did not reflect a discount. When the volume discounts were applied to prior sales, the sales tax payable account was debited, or decreased, to

reflect the tax due on the diminished sales price. The customer was issued a "credit memo" to indicate the discounted sales price and the reduced sales tax.

4. Typically, petitioner's agreements with its customers were verbal and no written contracts were placed in evidence. Mr. Fehr stated that the company's sizeable overhead costs required him to offer the volume discounts to increase the number of tons of asphalt he sold.

5. If a customer failed to reach the required volume of product to qualify for the discount, no discount would be applied.

6. In 2009, petitioner submitted a claim for refund based upon a bad debt. The Division undertook an audit of petitioner to determine if the claim was valid. Ultimately, a refund of $109,865.92 was granted, but the Division denied $25,020.20 of the claim.

7. The audit began on April 8, 2010 when the Division sent petitioner a request for books and records pertaining to its sales tax liability for the audit period. An additional request was made on May 26, 2011. The records produced were considered to be adequate and the Division decided to use a test period, September 1, 2009 through November 30, 2009, to review the sales records. The Division requested and received a test period audit method election from petitioner. The review completed by the Division discovered computational errors that resulted in an error rate of 0.0012371772, which, when applied to each quarter of the audit period, resulted in additional taxable sales of $14,512.00 and additional tax due of $1,251.66. At hearing, the Division conceded the issue of additional tax on sales as determined on audit. Therefore, the tax asserted in the Notice of Determination is reduced by $1,251.66.

8. A test period audit method election was also used for petitioner's expense purchases for various periods within 2008 and 2009. The test yielded additional purchases of $18,252.38 and

additional tax due of $1,574.27 for the audit period. Petitioner concedes the tax found due and it is no longer in issue.

9. Capital purchases were analyzed in detail for the audit period and resulted in no additional tax due.

10. The Division's audit included a review of petitioner's sales tax payable account. Here, the Division discovered that petitioner had made numerous adjustments to account for price reductions subsequent to the purchase and acceptance of asphalt by customers. The Division disallowed the reductions, or debits, made to the sales tax payable account attributable to discounts granted on prior sales. To expedite the audit of the sales tax payable account, the Division did not investigate or disallow debits to the account that were under $2,000.00.[2] The Division determined that petitioner had underreported $289,859.82 in sales tax for the audit period based on the adjustments made to the sales tax payable account after transactions had been consummated.

In the auditor's review of the sales tax payable account, the opening credit of $8,426.71 as of September 1, 2006 was not considered in her analysis and calculations. Thus, the Division disallowed petitioner's debit of $9,652.08, taken to neutralize the opening credit balance, which petitioner mistakenly believed the Division had considered. No explanation was given for the amount of petitioner's debit, which was in excess of the opening credit balance.

11. The Division issued to petitioner a statement of proposed audit change, which asserted additional sales and use tax for the audit period in the sum of $292,685.75 plus penalty and

[2]During the audit, inexplicably, the auditor allowed a debit to the sales tax payable account in the sum of $35,925.70 posted in August 2008. The auditor had no recollection of why this was allowed.

interest. The statement was returned by petitioner with the statement, "We disagree with the audit findings and with the Tax Department's position on the price adjustments."

12. The Division applied the allowable portion of the refund, $109,865.92, to the outstanding liability resulting from the audit.

13. As noted in Finding of Fact 6, petitioner filed a claim for refund, dated December 18, 2009. The Division issued a refund denial letter to petitioner, dated January 30, 2013, which indicated that $109,865.92 of the $134,886.12 requested had been granted, but denying the amount of $25,020.20. At hearing, petitioner conceded the propriety of the Division's modifications and withdrew its opposition to the conclusions reached in the denial letter. As noted in footnote 1, that matter is deemed resolved and closed (DTA No. 826279).

14. The Division issued to petitioner a Notice of Determination, dated March 15, 2013, based on the audit performed for the audit period, which asserted additional tax of $292,685.75 plus penalty and interest, and indicated credit for the allowable portion of the refund, $109,865.92. The additional tax was attributed to additional sales, $1,251.66, additional expense purchases, $1,574.27, and the disallowance of debits to the sales tax payable account, $289,859.82.

SUMMARY OF THE PARTIES' POSITIONS

15. Petitioner argues that the Division's denial of its debit to the sales tax payable account to write off the opening credit balance as of September 1, 2006 was in error. It contends that the opening credit balance accrued prior to the start of the audit period and therefore was beyond the allowable period of limitations. Although the debit made by petitioner to account for the credit balance was $9,652.08, it argues that the portion attributable to the opening credit balance of $8,426.71 should be allowed.

16. Petitioner maintains that the Division incorrectly denied its debits to the sales tax payable accounts to account for volume discounts on prior sales. Petitioner argues that it had to offer volume discounts to boost sales and pay its costly overhead. Further, petitioner notes that many asphalt jobs last months, if not years, and the volume discounts are therefore delayed by the nature of the industry.

17. Petitioner argues that the Tax Law with regard to the application of volume discounts is vague and confusing and must be resolved in favor of the taxpayer. In support of this position, petitioner notes that the auditor made a notation in her initial work papers that an August 2008 debit in the sales tax payable account in the sum of $35,925.70 was an allowable price adjustment for credit on the May 2008 return. Subsequently, the same debit was disallowed, indicating to petitioner that the law was not clear to the Division.

18. Petitioner believes that the law allows for a volume discount and the Division does not have the authority to limit petitioner's right to offer one. Petitioner believes that the Division's interpretation is unduly burdensome in that it permits a volume discount only when the volume is purchased all in the same transaction.

19. Petitioner argues that the Division's audit methodology was arbitrary and capricious because the auditor chose to ignore and not audit debits to the sales tax payable account that were below $2,000.00.

20. The Division contends that volume discounts are recognized when given at the time of the initial sale, citing to its regulation at 20 NYCRR 525.2 and the New York State Tax Bulletin, TB-ST-860. Those discounts applied later, which modified the sales prices, do not permit debits to the sales tax payable account.

21. The Division argues that the auditor was within her authority to eliminate debits to the sales tax payable account less than $2,000.00. She used the technique to expedite her investigation, and all eliminated debits were accepted as permissible and in the taxpayer's favor. The Division contends that her methodology did not make the entire audit arbitrary and capricious.

22. The Division counters petitioner's objection to the denial of the debit that was made to account for the opening credit balance in the sales tax payable account by pointing out that the auditor never considered the opening credit balance in her calculation of additional tax due, choosing to begin her analysis with a zero balance for the account as of September 1, 2006.

CONCLUSIONS OF LAW

A. The issues remaining for adjudication by this forum are those that resulted from the Division's audit of petitioner's business for the audit period and the issuance of the Notice of Determination. Since tax on additional sales was conceded by the Division (Finding of Fact 7) and additional expense purchases found by the Division were not challenged by petitioner (Finding of Fact 8), the unresolved dispute arises from the treatment of the adjustments made to the sales tax payable account.

B. Tax Law § 1105(a) imposes a sales tax on the receipts from every retail sale of tangible personal property. Retail sale is defined in Tax Law § 1101(b)(4) and 20 NYCRR 526.6 as the sale of tangible personal property to any person for any purpose. The regulation at 20 NYCRR 525.2(a)(2) reminds us of the nature of the sales tax:

> "[T]he sales tax is a 'transactions tax,' with the liability for the tax occurring at the time of the transaction. Generally, a taxed transaction is an act resulting in the receipt of the consideration for the transfer of title to or possession of tangible personal property or for the rendition of an enumerated service. The time or method

> of payment is generally immaterial, since the tax becomes due at the time of transfer of title to or possession of (or both) the property or the rendition of such service . . . ."

The regulations also provide that the sales tax is a "destination tax" where "[t]he point of delivery or the point at which possession is transferred by the vendor to the purchaser . . . controls both the tax incidence and the tax rate." (20 NYCRR 525.2[a][3].)

The is no question that petitioner was making retail sales of tangible personal property to its customers, who were charged a posted rate, usually pursuant to an oral agreement. Since the asphalt was transferred to purchasers' trucks on petitioner's site and then removed immediately by the purchasers, the sales tax was due then on the posted price, since title and possession of the product had been transferred. The time or method of payment was not material. (20 NYCRR 525.2[a][2].) In fact, petitioner's own invoices indicate this was how it viewed and characterized the transaction at the time it occurred, with the sales tax clearly stated to be due on the dollar value of the product purchased.

The Division recognizes that volume discounts offered by a vendor may reduce the purchase price, and thus the tax due (20 NYCRR 526.5[d][2]). The Division further elaborated on the volume discount in its Tax Bulletin, ST-860 (November 3, 2014), where it states that volume discounts offered at the time of sale will reduce the taxable receipt and that such discounts are subtracted before calculating the amount of sales tax due on the sale.

Petitioner's interpretation of when the tax became fixed differs from the Division's in that petitioner believes a volume discount can be applied at any time, thus leaving the moment of incidence of the tax in a suspended state, which potentially could extend for years or possibly never materialize. This is an untenable position.

The tax treatment of volume discounts has its genesis in Tax Law § 1101(b)(3), where a receipt is defined as the sale price of any property. The Division elaborated in its regulations, specifically permitting volume discounts as reductions to the purchase price, which resulted in a lower price and less sales tax. (20 NYCRR 526.5[d][2].) Read in conjunction with Tax Law §§ 1105(a) and 1101(b)(4) and the regulations at 20 NYCRR 525.2(a)(2) and (3), the clear intent of the statutes and regulations was to impose the sales tax at the time of the transfer of title and possession, i.e., the point in time that controls both the incidence and the tax rate. Petitioner has cited no authority for the adjustments it made to its sales tax payable account, sometimes years after the title and possession to its product had been transferred to its purchasers.

Petitioner's president was quite candid in his explanation for the structure of the transaction: petitioner wanted to offer the volume discounts to be competitive in the marketplace and meet its high overhead costs. However, petitioner was also aware that its customers could be lured by a competitor's lower price unless they had an incentive to remain with petitioner. That incentive was the volume discount, only available to customers when they met their volume goals. A customer could not stop ordering with petitioner prior to reaching the volume goal without being forced to pay the full posted price for all orders, as stated on their original invoices.

Once the goals were met, the discount was applied retroactively by means of credit memos and adjustments to the sales tax payable account, regardless of when the sale took place. The form of the transaction may have presented a good business strategy, but it was not a sound tax practice in light of the law and regulations discussed above. The sales tax was due and payable on the original invoice price, to which the volume discounts had not been applied (except in rare instances where it is presumed the discount was applied).

C. With regard to petitioner's attempt to debit the sales tax payable account to counterbalance the opening credit balance, dated September 1, 2006, which it believed the Division had included in its analysis of the account, the record clearly indicates that the opening credit balance was not included in the Division's audit of the account. The work sheets included in Division's Exhibit J plainly demonstrate that the opening credit balance was not audited or added to the sales tax payable totals. The auditor credibly testified that she did not consider, audit or use the opening credit balance in her analysis and began with a zero balance. Therefore, it is determined that the opening credit balance was not considered and the Division's denial of petitioner's attempt to debit the account was proper. As the Division noted, the debit claimed was in excess of the opening credit balance, but no explanation was offered to substantiate the sum. Therefore, denial of the entire debit was proper.

D. Petitioner has charged that the Division's audit lacked a rational basis because the auditor chose to ignore debits of $2,000.00 and below in her analysis of the sales tax payable account. Petitioner's objection to the elimination of these debits is contrary to its position, since every debit that was allowed had the effect of diminishing the additional tax petitioner owed. The auditor used her discretion in choosing to eliminate debits of less than $2,000.00 to expedite her analysis and concentrate on what she determined to be more substantial entries. She accepted as correct entries made by petitioner which, it can be safely assumed, petitioner supplied in good faith and believed to be true and correct.

The Division's analysis of the sales tax payable account was performed in detail. Its decision to accept certain entries as true and correct did not belie its obligation to review petitioner's complete and adequate records. (***Matter of Chartair, Inc. v. State Tax Commn.***, 65

AD2d 44, 46 [3rd Dept 1978]; ***cf***. ***Matter of Marine Midland Bank***, Tax Appeals Tribunal, May 13, 1993.)

E. The petition of Prima Asphalt Concrete, Inc., is denied and the Notice of Determination, dated March 15, 2013, as modified consistent with Findings of Fact 7 and 8, is sustained.

DATED: Albany, New York
February 25, 2016

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