

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition

of

UTOPIA SERVICE CENTER

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, 1981 through August 31, 1982.

DECISION
DTA NO. 801361

Petitioner, Utopia Service Center, 181-05 Horace Harding Boulevard, Flushing, New York 11365 filed an exception to the determination of the Administrative Law Judge issued on April 14, 1988 with respect to its 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, 1981 through August 31, 1982 (File No. 801361). Petitioner appeared by Sanford B. Potters, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Mark Volk, Esq., of counsel).

Both parties filed a brief on exception. Oral argument was not requested.

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

ISSUE

Whether the Division of Taxation properly determined petitioner's taxable sales based on information supplied by petitioner and petitioner's supplier, rather than performing a complete audit of petitioner's books and records.

FINDINGS OF FACT

We find the facts as stated by the Administrative Law Judge except that we modify findings of fact "4(c)" and "5(b)" as indicated below. The facts are as follows.

Petitioner, Utopia Service Center ("Utopia") was a gasoline service station located at 181-05 Horace Harding Boulevard, Flushing, New York. Utopia sold gasoline and performed automobile inspections and repairs. It was operated as a sole proprietorship by Vincent Casella.

A desk audit of Utopia was conducted by the Central Office Audit Bureau. The records available to the auditor were: a Filling Station Questionnaire completed by Utopia's accountant, Herbert Grodin; Mr. Casella's 1982 Resident Income Tax Return, including a copy of Federal Schedule C; purchase verification records for 1981 and 1982 obtained from Utopia's gasoline supplier, Mobil Oil Corporation ("Mobil"); Utopia's sales tax returns for the audit period; and a schedule of statewide average retail selling prices of regular gasoline prepared by the Miscellaneous Tax Section of the Division of Taxation.

The Filling Station Questionnaire contained the following declaration above Mr. Grodin's signature: "I/We certify that the information provided in this questionnaire accurately reflects the books and records of the business described here on [sic]."

To determine the accuracy and correctness of Utopia's filed sales tax returns, the auditor attempted to reconcile various information found on the documents described above.

On the Filling Station Questionnaire, Utopia reported purchasing 75,000 gallons of gasoline from Mobil in December 1981. The Mobil purchase verifications showed that Utopia purchased an average of 78,000 gallons of gasoline per month in 1981. On the same questionnaire, Utopia reported that the amount paid for all gasoline purchases in December 1981 was \$98,747.12, while Mobil reported the same information as \$94,341.00.

According to the questionnaire, Utopia had total gross sales in the quarterly period ended February 28, 1982 of approximately \$303,000.00 and had no tax exemption certificates on file. On its sales tax return for the period ended May 31, 1981, Utopia reported taxable sales and services of \$167,055.00.¹

We modify finding of fact "4(c)" of the Administrative Law Judge's determination to read as follows:

¹No reason was given for the comparison of different quarters. For the quarterly period ended February 28, 1982, Utopia reported taxable sales and services of \$217,440.00.

As reported on the questionnaire for the date February 18, 1984, Utopia's average selling price of gasoline (i.e., all grades of gasoline at both self-service and full service pumps) was \$1.325 per gallon, compared with the statewide average price of regular gasoline of \$1.277 per gallon.

On his 1982 Federal Schedule C, Mr. Casella reported gross receipts from Utopia of \$1,096,615.00. The auditor took three-quarters of this amount to reflect the nine months included in the sales tax period December 1, 1981 through August 31, 1982, arriving at a total of \$822,461.00. She compared this figure with Utopia's reported taxable sales of \$620,555.00 for the period December 1, 1981 through August 31, 1982, as shown on its New York State sales tax returns. The comparison disclosed a discrepancy of \$202,206.00.

Because of the disparities disclosed by her examination of the various documents filed on behalf of Utopia, the auditor deemed Utopia's sales tax returns to be incorrect and its books and records to be inadequate to verify Utopia's actual sales. Therefore, the auditor determined the amount of tax due from Utopia on the basis of information available to her.

Mobil's purchase verifications were used to calculate Utopia's average quarterly gasoline purchases. For the period March 1, 1981 through November 30, 1981, it was determined that Utopia purchased an average of 183,381 gallons of gasoline per quarter. For the period December 1, 1981 through August 31, 1982, it was determined that Utopia purchased an average of 212,358 gallons of gasoline per quarter.

Finding of fact "5(b)" of the Administrative Law Judge's determination is modified to read as follows:

The auditor determined that on February 18, 1984 Utopia's average gasoline selling price was approximately three percent higher than the statewide average selling price of regular gasoline. To determine Utopia's average taxable gasoline selling price for each quarterly period, she increased the statewide average selling price for a gallon of regular gasoline by three percent and reduced the result to adjust for excise taxes and State

sales tax included in the selling price.

Utopia's average taxable gasoline selling price (as calculated above) was applied to average gallons of gasoline purchased each quarter to determine audited gasoline sales.

The auditor increased audited gasoline sales by seven percent to determine Utopia's total audited sales. The seven percent figure was calculated from Utopia's Filling Station Questionnaire which showed that seven percent of Utopia's total sales were of sales other than gasoline.

The applicable sales tax rate was applied to audited taxable sales to determine sales tax due per quarter. Sales tax paid by Utopia was subtracted from sales tax due to determine total tax due of \$27,811.04.

On April 26, 1984, the Division issued to Utopia a Notice of Determination and Demand for Payment of Sales and Use Taxes Due for the period March 1, 1981 through August 31, 1982, assessing tax due in the amount of \$27,811.04 plus penalty and interest.

When preparing the Filling Station Questionnaire, Utopia's accountant did not calculate the information requested from Utopia's books and records. Instead, he supplied information which he estimated based on his familiarity with those books and records.

Mr. Casella recorded Utopia's daily business transactions on daily sheets, where he entered gasoline meter readings at the beginning and end of each day and the pump price of each grade of gasoline. The accountant summarized information from the daily sheets and transcribed the summaries in a general ledger which was used as a basis for determining sales tax due.

Twelve other gasoline service stations operated in an eight-block area in the vicinity of Utopia. There were so many stations on Horace Harding Boulevard that it was referred to as "Gasoline Alley".

Because of financial hardships experienced by Utopia, it received rent adjustments from Mobil in January 1982 and July 1983. To obtain approval for these adjustments, Utopia's Mobil sales representative prepared a Service Station Operating Analysis for each of those months. The two analyses provide the following pricing information:

	<u>January 1982</u>		<u>June 1983</u>	
	<u>Full</u>	<u>Self</u>	<u>Full</u>	<u>Self</u>
	<u>Service</u>	<u>Service</u>	<u>Service</u>	<u>Service</u>
Premium	149.9	147.9	146.9	---
Regular	134.9	129.9	126.9	---
Unleaded	139.9	137.9	131.9	---

The statewide average selling price of gasoline referred to in reference to the audit of Utopia is calculated by the Miscellaneous Tax Section from a quarterly survey of service stations throughout New York State. The price referred to is the price of regular gasoline including all taxes.

For the quarterly period ended February 28, 1982, the average statewide selling price of regular gasoline was \$1.353. For the quarterly period ended August 31, 1983, the average statewide selling price of regular gasoline was \$1.298.

On its Filling Station Questionnaire, Utopia reported the following gasoline selling prices on February 18, 1984:

<u>Grade</u>	<u>Self-Service</u>	<u>Full Service</u>
Regular	119.9	123.9
Unleaded	127.9	131.9
Super	143.9	147.9

On at least one occasion after the notice of determination was issued, Mr. Grodin requested that the Division conduct a complete audit of Utopia's books and records. Such an audit was not conducted.

OPINION

The Administrative Law Judge determined that the Division had a reasonable basis for its determination that Utopia's books and records were inadequate, i.e., the disparity between taxable sales reported on sales tax returns and gross sales reported on the Filling Station Questionnaire. Based on this conclusion the Administrative Law Judge determined the Division was authorized to resort to external indices in estimating the tax due and that the audit methodology employed was reasonable under these circumstances.

On exception petitioner argues that it had adequate books and records that were never examined by the Division. As a result, petitioner argues the Division's resort to estimate procedures

was arbitrary and capricious and lacked a rational basis.

In response, the Division of Taxation argues that its inability to reconcile the information provided by Utopia on the Filling Station Questionnaire with Utopia's sales tax returns indicated that petitioner's books and records were inadequate. In effect, the Division argues that the attempt to reconcile this information substituted for a detailed review of petitioner's books and records.

We reverse the determination of the Administrative Law Judge.

Our analysis begins with the principle that the Division's resort to external indices to estimate sales tax liability "must be founded upon an insufficiency of record keeping which makes it virtually impossible to verify taxable sales receipts and conduct a complete audit" (Matter of Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 46). To support its determination that a taxpayer's records are so insufficient that a complete audit is not required, the Division must make more than "a weak and casual" request for the relevant records (Christ Cella, Inc. v. State Tax Commn., 102 AD2d 352, 354). The first issue is then whether the Division made an adequate request for petitioner's records.

It is undisputed that the only request ever made for the petitioner's records was the request to complete the Filling Station Questionnaire. The record does not indicate what instruction accompanied the questionnaire. All we have before us is the questionnaire, as completed by petitioner's accountant, which sets forth gross sales information for each of the months December 1981, January 1982 and February 1982. Assuming that the request to complete the questionnaire is a request for the petitioner's records - in effect a request that the taxpayer conduct a self-audit - at the most, the questionnaire before us was a request for the records for the quarter ending February 28, 1982. Under Adamides v. Chu (134 AD2d 776), a request and an examination of records for one period does not support the conclusion that records for another period are inadequate. Accordingly, the Division's determination that petitioner's records were inadequate for all periods of the assessment other than the quarter ending February 28, 1982 is unsupported and the resort to estimate methods for these other periods was improper (Matter of Max Service Station, Tax Appeals Tribunal, September 29, 1988).

With respect to the quarter ending February 28, 1982, still assuming that the request to

complete the questionnaire is an adequate request for books and records, the next issue is whether the Division's examination of the information for this quarter supported its conclusion that the books and records were inadequate and that tax for this quarter could be estimated utilizing external indices (King Crab Restaurant, Inc. v. Chu, 134 AD2d 51). The information reported by petitioner on the questionnaire indicated that he had gross sales totalling approximately \$303,000.00 for the quarter. On its sales tax return for the same quarter petitioner reported taxable sales of \$217,440.00; petitioner did not show the amount of gross sales on the return. If this information is interpreted most negatively against petitioner, it indicates that an audit of petitioner's books and records would have revealed that petitioner underreported its taxable sales by \$85,560.00 (\$303,000.00 - \$217,440.00). This conclusion assumes, of course, that petitioner had no nontaxable sales and thus its gross sales equalled its taxable sales. The important point is that this information does not indicate that petitioner's books and records were inadequate, it only indicates that petitioner may have underreported its sales tax. However, the Division did not determine tax, for this quarter or any other, based on this discrepancy. Instead, the Division relied on this discrepancy to estimate tax based on information supplied by Mobil with respect to petitioner's purchases and by utilizing an estimated selling price. This reliance was incorrect. The law, section 1138 of the Tax Law, and the cases thereunder permit resort to external indices when the taxpayer's records are inadequate (Matter of Chartair, Inc. v. State Tax Commn., *supra*) or when a taxpayer refuses to respond to a request for records (Matter of Continental Arms v. State Tax Commn., 72 NY2d 976). The law does not authorize the use of external indices merely because the tax return is incorrect. Since there is nothing on the face of the completed questionnaire to indicate that petitioner's books and records were inadequate, we conclude that the Division did not have a sufficient basis to support this conclusion. Thus, the resort to external indices was also inappropriate for the quarter ending February 28, 1982 and the audit methodology employed was unreasonable.

Further, we find no basis in the record before us to adjust the tax for the quarter ending February 28, 1982 to an amount derived from the apparent discrepancy revealed by the petitioner on

its questionnaire. As found by the Administrative Law Judge, this information was not calculated by petitioner's accountant from Utopia's books and records but was instead estimated by the accountant based on his familiarity with the books and records. Accordingly, we conclude that it does not provide a basis to determine tax for this quarter.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Utopia Service Center is granted;
2. The determination of the Administrative Law Judge is reversed; and
3. The petition of Utopia Service Center is granted and the Notice of Determination issued on

April 26, 1984 is annulled.

Dated: Albany, New York
March 9, 1989

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner