

II. Whether petitioner's purchases of linens, uniforms, machinery parts and supplies were subject to sales and use taxes.

FINDINGS OF FACT

We find the facts as stated in the determination of the Administrative Law Judge and such facts are incorporated herein by this reference. They are summarized below. In addition to the facts found by the Administrative Law Judge, we find certain additional facts as indicated below.

On June 20, 1985, the Division of Taxation issued to petitioner, City Linen and Towel Supply Co., Inc., a Notice of Determination and Demand for Payment of Sales and Use Taxes Due, for the period June 1, 1981 through November 30, 1984, assessing taxes due in the amount of \$23,744.63 plus interest. The notice declared that the tax assessed had been estimated in accordance with the provisions of section 1138(a)(1) of the Tax Law.

Petitioner operated a linen supply business which supplied commercial establishments with clean linen such as hand towels and uniforms. A field audit of petitioner's operations began in January 1985. The auditor met with petitioner's president, Robert Ross, explained the nature of the audit and requested certain books and records. Mr. Ross referred the auditor to petitioner's bookkeeper who provided the auditor with sales journals, purchase journals, income tax returns and purchase invoices. A review of petitioner's purchase invoices disclosed that petitioner had not paid sales tax to its suppliers on its purchases of linens, machinery parts and supplies used in its business. Because the auditor considered these purchases to be subject to the imposition of sales tax, she prepared a tax assessment based on petitioner's failure to pay tax on its taxable purchases. The auditor's methodology and calculations are summarized below:

(a) Using the purchase invoices supplied, the auditor prepared a schedule of purchases detailing the following information: purchase invoice date, purchase invoice number, supplier's name, merchandise subject to tax, and amount subject to tax. She then added all taxable purchases and arrived at a total of \$339,216.24.

(b) The auditor then aggregated the purchases by calendar year. This resulted in taxable purchases of \$31,911.00 for the period June 1, 1981 through December 31, 1981, \$120,761.00 for the year 1982, \$101,792.00 for the year 1983 and \$84,743.00 for the period January 1, 1984 through November 30, 1984. Total taxable purchases calculated in this manner amounted to \$339,207.00. (The discrepancy in the totals is explained by the auditor's practice of rounding figures to the nearest whole dollar.)

(c) Annual taxable purchases were divided by the number of months in that portion of each calendar year included in the audit period. These average monthly purchases were multiplied by three (reflecting the three months in each sales tax quarter) and the resulting three-month figures were then attributed to corresponding sales tax quarters. This method of attributing taxable purchases to quarterly periods was described as "straightlining" the purchases.

(d) Total purchases as calculated above amounted to \$339,209.00. A tax rate of 7% was applied to purchases per quarter to determine total tax due from petitioner of \$23,744.63.

After the completion of the audit, the auditor provided Mr. Ross with an oral summary and explanation of her conclusions and a copy of her workpapers, including the detailed schedule of purchases. Mr. Ross forwarded this schedule to his accountant. At a tax conference, the accountant demonstrated that sales tax had been paid on total purchases of \$2,549.00 as shown on invoices from two suppliers. Based on these invoices, the Division of Taxation conceded that the total purchases should be reduced to \$336,653.00 with a tax due on that amount of \$23,565.71.

Petitioner submitted eight proposed findings of fact. Proposed findings 1, 2, 3, 4 and 7 were substantially incorporated into the Administrative Law Judge's determination. The remaining proposed findings were not accepted because they were not supported by the evidence.

The Tax Appeals Tribunal finds additional facts as follows.

Petitioner filed its petition for hearing on September 6, 1985. The Division's answer to the petition is dated March 9, 1987. The Division asserted that the box on the assessment notice indicating that the assessment was estimated was checked in error, and that the Division did not estimate the tax due (Division's Answer, paragraph "7").

In its reply, the petitioner denied the Division's assertion that the assessment notice was erroneously prepared and asserted that the proposed tax liability was estimated (Petitioner's reply, paragraphs "1" and "4").

The hearing before the Administrative Law Judge was held on September 16, 1987.

OPINION

It is the Division's position that the exact amount of tax due for the audit period was determined from a detailed review of petitioner's books and records, in particular petitioner's purchase invoices. While conceding that straightlining the purchases resulted in certain transactions being attributed to the wrong sales tax quarter, it asserts that the total amount of tax assessed for the audit period accurately reflects petitioner's liability as shown by its purchase invoices. While the Division concedes that the notice sent to petitioner erred in declaring that the tax assessment had been estimated, it contends that the error did not render the notice void in its entirety and did not prevent petitioner from challenging the assessment.

The petitioner asserts that straightlining the purchases was a method of estimating tax due and that the estimating of tax is not permitted where, as here, a taxpayer maintains adequate books and records from which the exact tax due can be computed, which books and records were made available to the Division. Furthermore, petitioner asserts that it was prevented by

the methodology employed from tracing any particular invoice to a particular sales tax quarter; and therefore, it was prevented from competently challenging the assessment.

In the alternative, petitioner asserts that, if the assessment was not estimated, the notice was misleading and prejudicial because it failed to adequately inform petitioner of the basis for the assessment.

The Administrative Law Judge determined that petitioner's liability was not estimated but resulted from a full audit of petitioner's books and records. The Administrative Law Judge also concluded that the notice of determination was in error with regard to how petitioner's liability was determined and that the method of straightlining was improper because it resulted in certain transactions being attributed to the wrong sales tax quarters; however, the petitioner was not stopped from effectively challenging the results of the audit by these errors. The Administrative Law Judge pointed out that the ability of the petitioner's accountant to identify certain purchase invoices where sales tax had been paid and to bring about a reduction in tax on that basis demonstrates that petitioner was fully capable of addressing any claimed errors in the audit. The Administrative Law Judge also concluded that petitioner's purchases were subject to sales and use taxes.

The Administrative Law Judge directed the Division to recalculate tax and interest due based upon actual purchases in each sales tax quarter.

The two primary issues confronted on this exception are (1) whether sales tax liability asserted against petitioner was estimated or resulted from a detailed audit of petitioner's books and records and (2) whether under the facts and circumstances of the case, petitioner's ability to

challenge the assessment was impaired by the actions of the Division. The final issue is whether the purchases were exempt from sales and use taxes.

We conclude that petitioner's asserted liability resulted from a detailed audit of its books and records and that petitioner's ability to challenge the assessment was not impaired by the actions of the Division. Accordingly, we sustain the determination of the Administrative Law Judge in its entirety.

We deal first with the audit methodology.

It is conceded by the Division that petitioner had adequate and complete books and records. It is uncontroverted that the Division did analyze each purchase invoice provided by petitioner in determining the assessment. It is also uncontroverted that the Division calculated petitioner's liability by "straightlining" the purchases, i.e., averaging purchases monthly and attributing these average monthly purchases to quarterly periods.

The straightlining was a means of allocating the aggregate liability and did not alter the basic nature of the Division's audit methodology, i.e., a detailed audit of petitioner's purchase invoices. In Matter of D.J.H. Construction, Inc. v. Chu (Supreme Court, Appellate Division, Third Department, December 1, 1988, Justice Levine) the Court, faced with the same method of calculation, concluded:

"Despite the fact that the notices concededly were inaccurate as to the tax deficiencies on a quarterly basis, because of the improper averaging of the sales and use taxes due for the entire audited periods, the totals were based, not on an estimate, but upon a detailed audit which was substantially accurate according to the information petitioner had then furnished the State auditor. The notices adequately apprised petitioner of the aggregate deficiencies asserted for the relevant periods and of the need to pursue its administrative remedies to contest the assessments. Thus, the September 1980 and June 1981 notices of determination validly complied with the statutory time requirements, as extended under petitioner's consents (see, Matter of Pepsico, Inc. v. Bouchard, 102 AD2d 1000, 1001)."

The only deleterious effect of straightlining was a miscalculation of the interest on the deficiency which was rectified by the Administrative Law Judge's direction to the Division to recalculate the tax and interest due on a quarterly basis.

We deal next with whether petitioner's ability to effectively challenge the assessment was impaired by the fact that the Notice indicated that tax was estimated. We conclude it was not.

First, petitioner was made aware of the Division's position that the Notice erroneously indicated that the liability was estimated nearly six months prior to hearing, through the Division's answer. Petitioner's reply to the answer denied the Division's assertion of error and reiterated the crux of petitioner's argument as presented in its petition, namely, that the Division's audit methodology was one of estimating petitioner's tax liability, not a detailed audit of petitioner's books and records.

Petitioner pursued this line of argument at hearing. Petitioner did not attempt to challenge the accuracy of the aggregate deficiency asserted against him for the period, or any part of it. Petitioner alleges that the method of assessment made it impossible to determine the exact purchases upon which the Division based its assessment. We disagree and conclude that petitioner chose not to utilize the information made available to it which would have allowed an item by item challenge to the tax assessed.

The audit workpapers (Department Exhibit H) provided to petitioner included a nine page schedule of purchases which detail each invoice by date, number, supplier, description of the purchase, and the amount of the purchase. The total of these scheduled purchases is \$339,216.24. The total purchases upon which tax was assessed was \$339,209. While there is a

discrepancy of \$7.24 between the two amounts, it is clear that the nine page schedule provided petitioner the precise information to challenge every portion of the assessment.

We acknowledge, as did the Administrative Law Judge, that the method of assessment incorrectly allocated purchases to particular quarters. However, given the specificity of the audit workpapers provided to the petitioner we do not see how this error in allocation precluded petitioner from determine the exact purchases at issue. We conclude that the petitioner elected not to challenge the assessment on a purchase by purchase basis.

We conclude that under the facts and circumstances herein, the notice served its statutory purpose of apprising the petitioner that tax was due and the need to pursue its administrative remedies to contest the assessments. (Pepsico, Inc. v. Bouchard, 102 AD2d 1000; D.J.H. Construction, Inc. v. Chu, *supra*.) We find no evidence that petitioner's ability to effectively challenge the assessment was impaired.

Lastly, we reject petitioner's argument that the purchases at issue were exempt from tax because they were used in a laundering service which is excluded from tax by section 1105(c)(3)(ii) of the Tax Law. As the Administrative Law Judge held, section 1105(a) of the Tax Law imposes sales tax on the receipts from every retail sale of tangible personal property unless otherwise provided by Article 28 of the Tax Law. An exemption from tax "must clearly appear, and the party claiming it must be able to point to some provision of law plainly giving the exemption" (People ex rel Savings Bank of New London v. Coleman, 135 NY 231, 234; see also, Matter of Grace v. State Tax Commn., 37 NY2d 193, 196). The petitioner has failed to point to such a provision and we conclude that petitioner has failed to satisfy its burden under section 1132(c) of the Tax Law to prove that the receipts at issue are not subject to tax.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of City Linen and Towel Supply Co., Inc. is denied;
2. The determination of the Administrative Law Judge is affirmed; and
3. The petition of City Linen and Towel Supply Co., Inc. is granted to

the extent indicated in conclusions of law "D" and "F" of the Administrative Law Judge's determination and the Division of Taxation is directed to modify the Notice of Determination issued on January 20, 1985 accordingly, but except as so granted is in all other respects denied.

Dated: Albany, New York
MAR 02, 1989

John P. Dugan
President

Francis R. Koenig
President