

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

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In the Matter of the Petition	:	
	:	
of	:	
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<b>RAEMART DRUGS, INC.</b>	:	DECISION
	:	DTA NO. 802772
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 April 1, 1981	:	
through February 29, 1984	:	

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Petitioner, Raemart Drugs, Inc., 1221 Avenue of the Americas, New York, New York 10020, filed an exception to the Administrative Law Judge's determination issued on September 28, 1987 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 April 1, 1981 through February 29, 1984 (File No. 802772). Petitioner appeared by Arnold B. Panzer, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Michael B. Infantino, Esq., of counsel).

Neither party filed a brief on this exception nor was oral argument requested.

***ISSUE***

Whether the Division of Taxation properly denied petitioner's claim for refund of sales taxes assertedly overpaid during the period April 1, 1981 through February 29, 1984.

***FINDINGS OF FACT***

We find the facts as stated in the Administrative Law Judge's determination and such facts are incorporated herein by this reference. Such facts may be summarized as follows.

Petitioner, Raemart Drugs, Inc., is a corporation engaged in the retail drug store business in New York City through three separate stores. In addition to its sale of prescription drugs, petitioner sells approximately 20,000 different items including cigarettes (both by the pack and carton).

On April 24, 1984, petitioner filed thirteen applications for credit or refund of state and local sales or use tax, spanning the period April 1, 1981 through February 29, 1984, seeking a refund of

sales tax paid for such period in the total amount of \$180,357.00, plus interest. Each application contained the following explanation as to the basis for the claim for refund:

"Taxpayer included the sales applicable to cigarettes as taxable volume. In addition payment of the tax applicable to the cigarette sales was then remitted within the quarterly report."

Petitioner subsequently reduced the refund claim to \$140,890.

Each day during the audit period, petitioner handled transactions involving approximately 5,000 different customers, and its cash registers yield a daily total of over 50 separate rolls of tape. The type of cash registers employed by petitioner are typical of those used in the retail drug store business. Such registers indicate when and how much sales tax has been added onto an item, but do not record the nature of the item sold.

During the period in question petitioner filed quarterly and part-quarterly sales and use tax returns. Petitioner computed its sales and use tax liability using a 58% taxable ratio applied to its gross sales to arrive at taxable sales. This taxable ratio was based upon the results of a field audit performed by the Division of Taxation, which audit covered prior periods, specifically September 1, 1976 through February 28, 1979. This prior audit had found a taxable ratio on petitioner's gross purchases of 58.427% and a markup thereon of 30.9%. The audit resulted in a finding of additional taxable sales of \$176,342.00, and additional sales tax due thereon of \$14,179.00, which petitioner had agreed to and paid. Petitioner had filed its sales tax returns on the basis of an estimated taxable ratio prior to the time of this audit. During the period involved in the instant refund claim, petitioner filed on the same basis, although using the higher taxable ratio (58%), as found by the Division of Taxation upon audit.

In order to assist its cash register operators in correctly identifying those items on which tax was to be charged and collected in accordance with the guidelines established in the prior audit, petitioner "color coded" its price stickers (subsequent to the above-described audit), such that all cigarettes and candy on which tax was to be collected bore one color and those items which were

tax free (other than newspapers and magazines) bore another. Petitioner instituted this system to help insure that tax was correctly added at the register.

In filing its returns petitioner, as noted, computed its tax liability based on a ratio of 58% of its gross sales. In addition, petitioner added to the tax on 58% of its sales, an additional amount computed as the tax due on its sales of cigarettes, notwithstanding that cigarette sales were included as part of the 58% of gross sales upon which tax was computed. Petitioner's accountant made no adjustment whatsoever in the computation of gross and taxable receipts to eliminate therefrom sales of cigarettes, to the effect that the tax collected by the petitioner with respect to the cigarettes which it actually sold during the taxable periods in issue was inadvertently reported and remitted twice with its returns.

Subsequent to the filing of the aforementioned refund applications, the Division of Taxation conducted an audit of petitioner's books and records for the period April 1, 1981 through November 30, 1984.<sup>1</sup> Petitioner had not maintained cash register tapes for such period, and the Division of Taxation conducted its audit utilizing a test period spanning March 1, 1984 through May 31, 1984. The auditor reviewed invoices for such period and determined a taxable ratio of 59.738%, which was applied to petitioner's gross purchases to arrive at taxable purchases for the audit period. A markup percentage was not calculated. Rather, taxable purchases, as determined, were marked up by 30.9% based on the markup percentage determined on the prior audit, thus resulting in audited taxable sales of \$19,035,934.00. This figure was compared to petitioner's reported taxable sales of \$20,525,368.00 resulting in an estimated overreported taxable sales of \$1,489,434.00, and a possible overreported sales tax payment of \$122,738.07. Based on the findings of this audit, the Division of Taxation accepted that no additional tax was due.

On August 12, 1985, the Division of Taxation notified petitioner in writing that its refund claims totalling \$180,357.00 were "denied in full, based on TSB-H-82(167.1)S, (That petitioner failed to maintain the records under section 1135 of the Tax Law, and in the absence of such records

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<sup>1</sup>This audit was a "large vendor" audit, and encompassed three periods beyond the periods for which refund is claimed.

petitioner cannot establish the exact amount of sales tax liability for the periods claimed for refund)."

Petitioner asserts, with respect to its method of reporting its sales tax liability, that given the nature of its business, the large number of different items sold and the volume of transactions, it is impractical if not impossible to separately record the nature of each item sold and to segregate by item whether an item is taxable or nontaxable. Petitioner asserts that cash registers which not only indicate whether an item is taxable but also indicate the individual nature of the item are impractical for use in petitioner's business due to their cost, and maintains that such cash registers are essentially used only in a relatively small number of supermarket chains with their principal function being to keep track of the store's inventory for stocking purposes. Thus, petitioner asserts it is impossible to determine its taxable sales from an item-by-item review of the cash register tapes and impractical to manually record at the time of sale the nature of each of the thousands of items being sold. Accordingly, petitioner maintains its method of computing, reporting and paying tax is the only practical and acceptable method available.

At the hearing, the auditor admitted that the only records which the taxpayer did not have available which might have been consulted in the course of the audit examination were cash register receipts. Petitioner possessed an essentially complete set of invoices<sup>2</sup>, and also cash receipts and cash disbursement journals, a general ledger, entry sheets, complete bank statements, Federal, State and City tax returns and related worksheets, sales tax returns, depreciation schedules, a check register, cancelled checks, and monthly bank statements.

Petitioner's accountant and one of petitioner's officers each testified that prior to the audit of its 1976-1979 sales tax returns (the audit in which the 58% taxable ratio was computed), it was always petitioner's practice to save, mark and store all cash register tapes. However, after allegedly being informed by the persons conducting the audit that they were not required to examine the cash register tapes, and had no interest in doing so, petitioner's principals concluded that cash register

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<sup>2</sup> Although there were a few invoices which the taxpayer was unable to produce, the auditor conceded that their significance was not such as to prevent him from determining petitioner's taxable sales "within his usual level of exactitude."

tapes were not the type of records required to be saved for audit purposes, and that it was pointless to attempt to save them for any longer period than was required for their own accounting purposes.

When questioned with respect to the significance of the absence of cash register tapes, the Division of Taxation's auditor stated that the availability of such tapes would not have affected the manner in which he would otherwise have conducted his audit, nor would their presence have been sufficient to establish taxpayer's right to a refund, since the tapes produced by petitioner's cash registers did not identify the particular items sold in each transaction. The auditor also stated that the exact amount of the tax collected from customers could not be determined even in theory on the basis of the cash register tapes since no tax would be indicated on the tapes with respect to cigarette sales.

### ***OPINION***

Refunds of sales tax are authorized by Tax Law, section 1139(a) for amounts of tax erroneously paid to the Division of Taxation. Petitioner's claim for a refund was denied by the Administrative Law Judge because petitioner could not establish his exact tax liability and, thus, could not prove the amount of any erroneous payment. We affirm the Administrative Law Judge's determination.

The crucial fact in this case is that petitioner did not maintain records of each sale, as required by Tax Law §1135, such that a determination of its exact tax liability was possible. A determination of exact tax liability is a condition precedent to obtaining a refund (Matter of Saltzman v. State Tax Commn., 101 AD2d 910). Since petitioner could not determine its exact liability, its refund claim was properly denied.

Petitioner argues that it should be able to estimate its tax liability, and thus its refund, utilizing procedures that the Division of Taxation would utilize on audit. We disagree.

As stated by the Administrative Law Judge, audit procedures to estimate tax are authorized by Tax Law, section 1138 and the cases thereunder only when the vendor has failed to maintain books and records adequate to establish the exact amount of tax due (see, e.g., Matter of Urban Liquors, Inc. v. State Tax Commn., 90 AD2d 576; Matter of Licata v. Chu, 64 NY2d 873; Matter of Grant v. Joseph, 2 NY2d 196.) Estimates by the Division of tax liability are acceptable only on the

principle that "where the taxpayers own failure to maintain proper records prevents exactness in determination of sales tax liability, exactness is not required." (Matter of Meyer v. State Tax Commn., 61 AD2d 223, 228, lv denied 44 NY2d 645.)

Petitioner's position which would reverse this principle by allowing the vendor who fails to keep adequate books and records to estimate a tax refund is not sanctioned by the Tax Law.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of petitioner, Raemart Drugs, Inc., is in all respects denied;
2. The determination of the Administrative Law Judge is affirmed; and
3. The petition of Raemart Drugs, Inc. is in all respects denied and the denial of petitioner's claim for a refund is sustained.

Dated: Albany, New York  
July 8, 1988

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

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