STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition of **MGK CONSTRUCTORS** for Revision of Determinations or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Periods June 1, 1986 through August 31, 1986 and June 1, 1987 through November 30, 1987	:	DECISION DTA Nos. 807262, 807881 and 807882
In the Matter of the Petitions of **MGK CONSTRUCTORS** for Revision of Determinations or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period March 1, 1983 through February 28, 1988	:	

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on January 17, 1991 with respect to the petitions of MGK Constructors, 1 Lafayette Place, Greenwich, Connecticut 06830 for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the periods June 1, 1986 through August 31, 1986 and June 1, 1987 through November 30, 1987, and for the period March 1, 1983 through February 28, 1988. Petitioner appeared by Charles Slepian, Esq. and Herman Soloway, C.P.A. The Division of Taxation appeared by William F. Collins, Esq. (Carroll R. Jenkins, Esq., of counsel).

The Division of Taxation filed a brief in support of its exception. Petitioner filed a brief in opposition. Oral argument, at the request of the Division of Taxation, was heard on September 5, 1991.

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

ISSUES

I. Whether the issuance of a notice and demand for payment of certain penalties and interest due under Article 28, rather than a notice of determination, is insufficient to assert these penalties and interest.

II. Whether petitioner has demonstrated reasonable cause and the absence of willful neglect, thereby justifying remittance of the penalties and interest imposed for late filed sales taxes.

III. Whether the New York City sales tax on protective and related services imposed by the Administrative Code of the City of New York § 11-2040(a)(2) (imposed prior to September 1, 1986 by Administrative Code § BB46-2.0[a][2]) is due on the sale of guard services to petitioner, a construction contractor, who is performing work for the City of New York.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "8," "10," and "17" which have been modified. We also make an additional finding of fact. The Administrative Law Judge's findings of fact, the modified findings of fact, and the additional finding of fact are set forth below.

Petitioner, MGK Constructors, filed a petition (File No. 807262) on August 21, 1989 protesting three notices and demands for payment of sales and use taxes due (D8612089980 for the quarter ending August 31, 1986; D8712124534 for the quarter ending August 31, 1987; and S8804121289 for the quarter ending November 30, 1987) each dated April 11, 1988.

A request for a conference was made on January 13, 1989 but was found untimely by a conciliation conferee on June 9, 1989. The Division of Taxation has withdrawn that objection and any further objection that the petition was untimely.

These notices were paid in full but petitioner challenges the penalties shown thereon totaling $17,758.32.

Petitioner filed a petition (File No. 807881) on February 12, 1990 protesting two notices of determination (S881230000L and S881230003L) issued December 30, 1988 and eleven notices and demands for payment issued at various times (three of the notices and demands for payment are the three notices which are the subject of the petition in case number 807262 [see above]).

One notice of determination (S881230000L) is for the quarter ending May 31, 1983, the two quarters ending May 31, 1984, the quarter ending November 30, 1984, the two quarters ending August 31, 1985, the quarter ending February 28, 1986 and the quarter ending August 31, 1986. The other notice of determination (S881230003L) is for the quarter ending August 31, 1985 and is for omnibus penalty under Tax Law § 1145(a)(1)(vi) only.

A timely request for a conciliation conference with respect to the notices of determination was made on January 17, 1989 and the requests were denied on December 8, 1989.

The notices of determination showed that the amount of tax had been paid but the amount of penalty and interest had not been paid.

The eleven notices and demands for payment which are contested by this petition are as follows:

Notice Number	Period Ending	Date Issued
D8601090585	August 31, 1985	January 13, 1988
D8604031747	November 30, 1985	April 11, 1988
D8605232112	February 28, 1986	January 13, 1988
D8609143053	May 31, 1986	September 21, 1987
*D8612089980	August 31, 1986	April 11, 1988
D8703019119	November 30, 1986	September 26, 1988
D8706171465	February 28, 1987	September 26, 1988
D8709258657	May 31, 1987	September 26, 1988
*D8712124534	August 31, 1987	April 11, 1988
*S8804121289	November 30, 1987	April 11, 1988
S8810312142	February 28, 1988	October 31, 1988

*These determinations are included also in petition 807262.

All notices and demands for payment with one exception, show that the amount of tax due had been paid, but that the amount of penalty and interest had not been paid. The exception is

the last notice, S8810312142, which shows tax due of $8,598.21, penalty of $1,075.30 and interest of $488.57 but on which only $2,977.88 was paid.

We find an additional finding of fact to read as follows:

> The notices and demand were issued after petitioner late-filed the returns and paid the tax. Subsequently, the additional interest and penalties were paid in full under protest on December 23, 1988. At that time a request for refund was made.[1]

A petition (File No. 807882) was filed on February 12, 1990 protesting two notices of determination and demands for payment of sales and use taxes due each issued on December 30, 1988. One notice of determination (S881230001L) was for the period March 1, 1983 through November 30, 1986 (omitting, however, the quarter ending August 31, 1983) and was in the amount of $50,497.37, plus penalty of $13,994.27 and interest of $24,547.31, for a total amount due of $89,038.95. The other notice of determination (S881230002L) was for the period December 1, 1986 through February 28, 1988 and was in the amount of $17,971.67, plus penalty of $4,466.74 and interest of $3,031.14, for a total amount due of $25,469.55.

A conciliation conference was timely requested on January 17, 1989, but the request was denied on December 8, 1989.

The notices show that all amounts due have been fully paid.

Petitioner had executed consents which extended the time within which the tax due may be determined. These consents were as follows:

(a) A consent executed on December 20, 1986 that the amount of taxes due for the period September 1, 1983 through February 28, 1984 may be determined on or before June 20, 1987.

(b) A consent executed on June 18, 1987 that the amount of taxes due for the period September 1, 1983 through May 31, 1984 may be determined on or before September 20, 1987.

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[1]This fact was added to more fully reflect the record.

(c) A consent executed on August 21, 1987 that the amount of taxes due for the period September 1, 1983 through August 31, 1984 may be determined on or before December 20, 1987.

(d) A consent executed on December 18, 1987 that the amount of taxes due for the period September 1, 1983 through February 28, 1985 may be determined on or before June 20, 1988.

(e) A consent executed on May 20, 1988 that the amount of taxes due for the period September 1, 1983 through August 31, 1985 may be determined on or before December 20, 1988.

(f) A consent executed on November 17, 1988 that the amount of taxes due for the period September 1, 1983 through February 28, 1986 may be determined on or before June 20, 1989.

Petitioner, MGK Constructors, of Greenwich, Connecticut is a joint venture composed of MacLean Grove & Company, Inc., Grow Tunneling Corp., Kiewitt Construction Co. and Morrison Knudsen Company, Inc. Its managing partner is MacLean Grove & Company, Inc. also of Greenwich, Connecticut.

Petitioner pays sales and use taxes to New York under a direct pay permit under Tax Law § 1132(c) and so does not pay tax on its purchases from its vendors.

Petitioner is a very well-capitalized business and has never had a cash-flow problem. At least one of its members is a "big board" member.

Petitioner failed to timely file returns and pay sales and use taxes for several periods. These are the periods for which the notices of determination and the notices and demands for payment described above have been issued. Petitioner has, however, now filed such returns and paid the taxes due thereon.

ABATEMENT OF PENALTIES

The books and the tax returns of petitioner were prepared by Mr. Lou Johnston, described at times as the comptroller of petitioner. Lou Johnston was employed by MacLean Grove and Company, Inc. around 1974. His father had been a very respected senior vice-president of MacLean Grove. Lou Johnston started as a clerical employee but rapidly entered computer work and came to be in charge of all clerical functions, including preparing tax returns. His work had involved three construction contracts prior to the one here involved.

Mr. Johnston was supervised by Mr. Nadel (who was also president of MacLean Grove) and by Mr. Simoni, described as the "principals" of the joint venture. This supervision was informal only and no written reports were required.

We modify finding of fact "8" of the Administrative Law Judge's determination to read as follows:

> Petitioner had arranged for periodic audits of its financial affairs. An audit was made by Blau, Soloway, Goldstein and Company, CPA's. The audits were done quarterly at first and annually in later years. That firm had noticed slight irregularities in the bookkeeping of petitioner. The first time a problem occurred was for the period ending August 1983. It was dismissed without mention by the auditors, as they considered it to be a one time occurrence. In mid-1987 the problems again occurred, and at that time Mr. Johnston was informed that such practices must stop. At that time the auditors also informed a superior of Mr. Johnston that Mr. Johnston would have to be monitored concerning the filing of returns.[2]

Petitioner knew nothing of any delay or failure to file or pay its sales or use taxes prior to the day when its employee, Mr. Johnston, disappeared.

We modify finding of fact "10" of the Administrative Law Judge's determination to read as follows:

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[2]The Administrative Law Judge's finding of fact "8" read as follows:

> "Petitioner had arranged for periodic audits of its financial affairs. An audit was made by Blau, Soloway, Goldstein and Company, CPA's. The audits were done quarterly at first and annually in later years. That firm had noticed slight irregularities in the bookkeeping of petitioner but had dealt only with Mr. Johnston and had not reported any problem to anyone else employed by petitioner."

This fact was modified to more accurately reflect the record.

> The auditor of the Division of Taxation first tried to contact petitioner by writing to Mr. Johnston on September 17, 1986. He persisted in this with no result until December 7, 1987 when he went, unannounced, to petitioner's offices. Mr. Johnston said he was busy and he would telephone him. The auditor left and returned on January 27, 1988 to begin the audit. At this time the auditor was informed that Mr. Johnston had been hospitalized; a Mr. Bastone helped in getting the audit started.[3]

Petitioner discovered after the disappearance of Lou Johnston that many of its suppliers had not been paid. Some had failed to complain because of the very good reputation of petitioner. It also found sales taxes unfiled and unpaid.

Petitioner's officers found that Mr. Johnston had a "substance abuse" problem and they believe that he is under treatment.

PROTECTIVE SERVICES

Petitioner was the successful bidder with the City of New York Department of Environmental Protection, Bureau of Water Supply, for the building of a part of a tunnel under the East River.

With respect to sales taxes, the contract provides as follows:

> "Article XXXVII...
>
> The Bureau of Water Supply of the Department of Environmental Protection is an exempt organization under the New York State Tax Law and is exempt from the payment of Sales Taxes for materials and supplies incorporated in this project as an integral part thereof. The Contractor should not include in his prices such Sales or Compensating Use Taxes of the State of New York and its cities and counties."

The contract, known as contract 521B, provided for security guard services in the quantity of 14,400 man-days.

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[3]The Administrative Law Judge's finding of fact "10" read as follows:

> "The auditor of the Division of Taxation first tried to contact petitioner by writing to Mr. Johnston on September 17, 1986. He persisted in this with no result until December 7, 1987 when he went unannounced to petitioner's offices. Mr. Johnston said he was busy and he would telephone him. The auditor left and did not get back until May 2, 1988. By this time, the auditor found that Mr. Johnston had left the company and he dealt with a Mr. Plotkin, an office manager."

This fact was modified to more accurately reflect the record.

The guard services started on March 1, 1983 and continued until February 28, 1988.

The guards were supplied to petitioner by a firm, Sheldon Martin Associates, which was on a list of "local business enterprises" furnished by the City of New York.

We modify finding of fact "17" of the Administrative Law Judge's determination to read as follows:

> New York City engineers and inspectors were on duty at the job site at all times. During the project, the security guards were sometimes positioned by a New York City employee. Under the terms of the contract with the City, the guard service was not to be used by petitioner to guard petitioner's property. A specific request for the guards to protect the cars of petitioner's employees was denied by the City.[4]

Petitioner received from the City the cost it paid for the services plus a percentage allowance for administrative costs and profit.

OPINION

The Administrative Law Judge determined that the issuance of notices and demand is invalid to assert penalties and additional interest for the late payment of tax, as the assertion of such penalties and interest under Tax Law § 1145(a) without a notice of determination is invalid. Further, the Administrative Law Judge held that the penalties and the additional interest asserted with respect to the late filed sales taxes should be remitted, as petitioner has demonstrated reasonable cause and the lack of willful neglect. Additionally, the Administrative Law Judge found that the purchase of guard services was exempt from tax, as the sale to petitioner constituted a sale for resale, and that 20 NYCRR 541.3(d)(2)(iv) and 20 NYCRR 541.3(d)(4) were not applicable to the instant situation. Moreover, the Administrative Law Judge ruled that the regulations of the Division of Taxation (hereinafter the "Division"), which require more specificity in a sales contract than does the statute itself, are invalid.

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[4]The Administrative Law Judge's finding of fact "17" read as follows:

> "New York City engineers and inspectors were on duty at the job site at all times. A New York City employee directed where the security guards would be posted. The City would not authorize the guarding of employees' cars or of petitioner's property."

This fact was modified to more accurately reflect the record.

On exception, the Division makes several assertions. First, that the purchase of the guard services was not for resale, and that this issue was neither raised nor addressed by either party at the administrative hearing. Second, that the penalties were properly asserted by the issuance of the notices and demand for payment. On this point, the Division states that the sufficiency of the notices and demand for payment was never an issue; rather, the parties had agreed that the only issue was the existence of reasonable cause. Third, that petitioner has failed to demonstrate reasonable cause to justify the abatement of penalties and interest. Finally, that the payments for the guard services were taxable because petitioner was an independent contractor, not an agent, in its contract with the City of New York, in general, and, in particular, with regard to the provision of guard services.

In opposition, petitioner asserts that, under the contract, petitioner was at all times acting as an agent of the City of New York, including when petitioner fulfilled its contractual obligation to secure guard services. Further, that the Administrative Law Judge was correct in finding the purchase of guard services excluded from tax, as the purchase was made for resale purposes. Additionally, that no tax liability should be imposed because New York City, an exempt entity, is the end user of the guard services. Finally, petitioner argues that it has established reasonable cause and the absence of willful neglect, justifying the abatement of the applicable penalties and interest.

We reverse the determination of the Administrative Law Judge.

The first issue is whether the issuance of a notice and demand for payment is sufficient to assess penalties and interest due. Tax Law § 1138 states that a notice of determination shall be issued: where no return has been filed, where the return filed is incorrect or insufficient, or where the tax commission believes that the collection of an assessment may be jeopardized by delay (Tax Law § 1138[a][1] and [b]). The Court of Appeals has held that these are the only instances where a notice of determination is appropriate (Matter of Parsons v. State Tax Commn., 34 NY2d 190, 356 NYS2d 593; see also, Matter of Hall v. State Tax Commn, 108 AD2d 488, 489 NYS2d 787). Since our facts involve the late filing of a correct return, a circumstance not

covered by Tax Law § 1138(a)(1), a notice of determination would not have been appropriate. Therefore, the issuance of a notice and demand for payment was proper in this situation.

The next question concerns whether petitioner's late payment of sales tax was due to reasonable cause and the absence of willful neglect.

Tax Law § 1145(a)(1)(iii) states:

> "If the commissioner of taxation and finance determines that such failure or delay [to file a return or pay over tax] was due to reasonable cause and not due to willful neglect, he shall remit all of such penalty and that portion of such interest that exceeds the interest that would be payable if such interest were computed at the underpayment rate set by the commissioner of taxation and finance pursuant to section eleven hundred forty-two. The commissioner shall promulgate rules and regulations as to what constitutes reasonable cause."

The relevant provisions[5] of the regulation state:

> "(c) The following exemplify grounds for reasonable cause, where clearly established by or on behalf of the taxpayer or other person.
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> "(1) The death or serious illness of . . . [an] employee or other representative of the taxpayer . . ., which precluded timely compliance, may constitute reasonable cause, provided that:
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> "(i) in the case of the failure to file any return, the applicable return is filed; or
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> "(ii) in the case of the failure to pay or pay over any tax, such amount is paid or paid over, within a justifiable period of time after the death, illness or absence. A justifiable period of time is that period which is substantiated by or on behalf of the taxpayer of [sic] such other person liable for penalty, as a reasonable period of time for filing the return and/or for paying any tax based on the facts and circumstances in each case.
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> * * *
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> "(5) Any other cause for delinquency which would appear to a person of ordinary prudence and intelligence as a reasonable cause for delay and which clearly indicates an absence of willful neglect may be determined to be reasonable cause. Ignorance of the law, however, will not be considered as a basis for reasonable cause" (20 NYCRR 536.5[c][1] and [5]).

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[5]Petitioner has not expressly stated the basis for its allegation of reasonable cause and lack of willful neglect. We will address 20 NYCRR 536.5(c)(1) and (5), as these sections seem most applicable to the facts of this case.

We find petitioner has not shown that its actions constitute reasonable cause and the lack of willful neglect.

Petitioner has suggested that Mr. Johnston's circumstances led to the delays in filing and payment of taxes, but that, once the deficiencies were revealed, petitioner satisfied those obligations promptly. Although petitioner correctly states that it filed all returns and paid all taxes due when notified by the auditors, this action does not satisfy the "justifiable period" requirement of 20 NYCRR 536.5(c)(1), as some of the amounts due were delinquent for several years.

Rather, the critical factor in this issue concerns the conduct of petitioner's comptroller, Mr. Johnston, who was able to manipulate the filing and payment of returns for years before being discovered. The fact that Mr. Johnston successfully concealed these filing and payment inconsistencies does not relieve MGK of its liability. The lack of control procedures in petitioner's organization allowed Mr. Johnston to conceal his improper handling of the filing and payment of returns, and further allowed him to be the sole representative of petitioner's organization which dealt with, or avoided dealing with (see, Hearing Tr., pp. 39-40; Exhibit "G-1," auditor's notes), the Division. The existence of proper internal review procedures could have prevented such manipulations or, at least, could have demonstrated an effort by management to take steps to prevent such conduct (see, Hearing Tr., pp. 125-127; cf., Universal Concrete Prods. Corp. v. United States, 90-2 USTC ¶ 50,440 ["a corporation's failure to implement internal checks and controls over the employee responsible for tax obligations demonstrates a lack of ordinary business care and prudence and, as such, negates a claim that late filings, deposits, and payments are due to reasonable cause"]).

This lack of internal control mechanisms is even more unreasonable given that, at some point in 1987, MGK had been notified by its auditors (Blau, Soloway, Goldstein and Co., CPA's) of the need to supervise Mr. Johnston's filing of returns (see, Hearing Tr., pp. 157-158). In spite of this notice, MGK had taken no steps to supervise Mr. Johnston as of the auditor's December 7,

1987 visit to the business, nor as of the January 27, 1988 start of the audit. Failure to institute and maintain such internal controls is unreasonable and leaves the organization open to liability.

The final question is whether the guard services required by the construction contract between petitioner and New York City constitute taxable services, or are excluded from tax based upon one of two alternative theories.

Pursuant to the authority granted by Tax Law § 1212-A(h)(2)(B), the Administrative Code of the City of New York imposes a tax on the sale of protective services. Specifically,

> "(a) . . . there is hereby imposed within the city and there shall be paid a tax at the rate of four per cent upon the receipts of every sale, except for resale, of the following services . . . :
>
> * * *
>
> "2. Protective and detective services, including, but not limited to, all services provided by or through alarm or protective systems of every nature, including, but not limited to, protection against burglary, theft, fire, water damage or any malfunction of industrial processes or any other malfunction of or damage to property or injury to persons, detective agencies, armored car services and guard, patrol and watchman services of every nature, whether or not any tangible personal property is transferred in conjunction therewith . . ." (New York § 11-2040[a][2] [formerly § BB46-2.0(a)(2) prior to 9/1/86], emphasis added).

We reverse the Administrative Law Judge and find that petitioner is liable for sales tax on the guard services.

Petitioner's contract with the City of New York was for the construction of a water tunnel, not for the provision of guard services.[6] Though guard services were expressly required as a condition of the contract, this condition simply constitutes, in a general sense, another specification set forth by the City. The express provision for this service does not change its essential nature, i.e., one of many expense items which are necessary to satisfy the contractual obligation of constructing a water tunnel. In addition, the contract provision covering the City

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[6]Exhibit 1, page 49 states:

"CONTRACT 521B

"For the construction of a part of City Tunnel No. 3,
Stage 1, in the Borough of Manhattan, New York, N.Y."

exemption from sales tax is limited to "materials and supplies incorporated into the project" (Exhibit "1," p. 89, article XXXVII).

The Administrative Law Judge found that the purchase of the guard services by petitioner constituted a sale for resale. We disagree.

The regulations addressing the resale exclusion state:

> "(1) Where a person, in the course of his business operations, purchases tangible personal property or services which he intends to sell, either in the form in which purchased, or as a component part of other property or services, the property or services which he has purchased will be considered as purchased for resale, and therefore not subject to tax until he has transferred the property to his customer.
>
> "(2) A sale for resale will be recognized only if the vendor receives a properly completed resale certificate" (20 NYCRR 526.6[c][1] and [2]).

We conclude that no resale of the guard services occurred between petitioner and the City of New York. This decision is primarily based on the holding in Matter of Laux Adv. v. Tully (67 AD2d 1066, 414 NYS2d 53).

Laux Adv. concerned whether an advertising agency had to pay sales tax on materials and services used to produce "mechanicals" (a "mechanical" is a piece of art work which represents a completed advertisement). Photo negatives were made of the mechanicals which were approved by the customer. The negatives were then sent to the advertising media and the mechanicals were returned to the advertising agency (Matter of Laux Adv. v. Tully, supra). In Laux Adv., the court upheld the tax commission's assessment of sales tax on the materials and services purchased, stating that "[the] petitioner's purchase of materials [and services] to prepare mechanicals was not for the primary purpose of reselling them to the customers but rather for petitioner to place advertisements in publications for its customers . . ." (Matter of Laux Adv. v. Tully, supra, 414 NYS2d 53, 54). Similarly, the provision of guard services was not for the purpose of reselling them to the City, but rather to satisfy a contractual requirement, thereby allowing petitioner to fulfill its obligation to build a water tunnel. In our view, the guard services were in the nature of an item of overhead, rather than a purchase for resale (see, Matter of

Niagara Lubricant Co. v. State Tax Commn., 120 AD2d 885, 502 NYS2d 312, lv denied 68 NY2d 607, 506 NYS2d 1031, citing Matter of Celestial Food v. State Tax Commn., 63 NY2d 1020, 484 NYS2d 509).

Moreover, no resale certificate has been offered, nor has petitioner even alleged that any resale certificate was presented for the guard services.

In sum, petitioner did not sell the guard services to the City of New York; the guard services were used by petitioner in its completion of the contract.

We now address petitioner's assertion that it was acting as an agent of the City of New York, or, as petitioner also states the argument, that the City was the end user of the services.

When acting as a purchaser, user, or consumer, the City of New York is not subject to sales tax (Tax Law § 1116[a][1]; see, 20 NYCRR 529.2[b]). A contractor acting as an agent of the City would likewise not be subject to sales tax (see, 20 NYCRR 541.2[c]; 20 NYCRR 529.2[b]). Petitioner alleges that it was acting as an agent of New York City for the purpose of securing protective guard services for the construction site and, therefore, qualifies for an exemption.

As a general rule, statutes which provide for exemptions from tax must be strictly construed, and the taxpayer must clearly demonstrate that it is entitled to the exemption (Matter of Lever v. New York State Tax Commn., 144 AD2d 751, 535 NYS2d 158). Petitioner has not done so in this case.

Preliminarily, we reject the Division's application of 20 NYCRR 541.3(d)(4). The first line of this regulation limits its applicability to exempt organizations identified under Tax Law § 1116(a)(3)-(6). As New York City is an exempt organization pursuant to Tax Law § 1116(a)(1), it clearly is not subject to the criteria set out in 20 NYCRR § 541.3(d)(4).[7] Therefore, since no regulation addresses exempt organizations identified in Tax Law § 1116(a)(1) and (2), we must resort to general principles of agency.

[7]As the regulations are inapplicable to the case before us, we find it unnecessary to address the Administrative Law Judge's holding regarding their validity.

> "To establish an agency or representative relationship there must be a manifestation that petitioners consented to act on behalf of their clients, subject to the latter's control and that the clients authorized this fiduciary relationship" (Matter of Hooper Holmes, Inc. v. Wetzler, 152 AD2d 871, 544 NYS2d 233, 235, lv denied 75 NY2d 706, 552 NYS2d 929).

Applying this principle, we determine that there was no agency relationship between petitioner and the City of New York. Several factors lead us to this conclusion. Initially, petitioner has been unable to point to an express clause in the contract[8] or any document executed at the time

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[8]At the hearing the parties referred to "the contract" as being the documents presented as Exhibit "1." However, only twelve select pages of the contract make up Exhibit "1." During the hearing this discrepancy is realized and the full contract is discussed:

(Division's Counsel) Q. "Then let's go on to the next question, or do you want to have more time to look [through Exhibit "1"] for the first answer or--
(Edward Plotkin) A. "I--okay.
Q. "--are you just--
A. "Just so you understand, this is not the complete contract. This portion that you see are those items that pertain to sales tax. The complete contract is a document of over 400 pages.
Q. "This is not the complete contract?
A. "No.

* * *

Q. "Mr. Plotkin, so you've said you couldn't find anything in the contract itself where you were designated as their agent. Is that what you said?
A. "I would have to read the whole document again. What I have here [Exhibit "1"], I would have to do this quickly. But again, it's 400 pages long and I just don't remember.
Q. "It doesn't help us much. I mean, we need to know. That's an important item.
Petitioner's counsel: "Well, he has already said, Your Honor, that he does not recollect.
Mr. Plotkin: "That's correct.
Petitioner's counsel: "And we will provide a full copy of the contract for counsel and he can look through it, if he likes, at his leisure.
ALJ: "I would--
Petitioner's counsel: "And for the court.
Mr. Plotkin: "I will run two sets, one for you and one for the court.
Division's counsel: "It's important for the court to have it at his side when he's rendering his opinion" (Hearing Tr., pp. 90; 95-96, respectively).

We determine that the representation of Exhibit "1" as "the contract" (Hearing Tr., pp. 55-56), in conjunction with the discussion at the hearing set out above, provide sufficient grounds to consider the entire 404 page document as having been entered into evidence, notwithstanding the failure of both parties to formally introduce the document at hearing or request that the record remain open for such purpose. Therefore, we find the document to be part of the record and properly before us (see, 20 NYCRR 3000.11[e][1], 20 NYCRR 3000.13[a][3]).

the contract was entered into which states that petitioner and the City of New York considered their relationship regarding the guard services to be one of agency (cf., Kern-Limerick, Inc. v. Scurlock, 347 US 110, 119-120 [where the Supreme Court addressed the relationship between a contractor and the Federal government regarding liability for State sales tax. The court found that the government's designation of the contractor as purchasing agent, in accordance with the contract arrangements, was consistently and expressly set out in the request for bids and purchase orders; therefore, the sales were exempt from tax]; see also, Matter of Sea-Land Restoration, State Tax Commn., July 1, 1985). Further, the contract does not vest the City with the level of control over the performance of petitioner's work that would indicate an agency relationship.

Second, several terms of the contract contradict the existence of an agency relationship. Specifically, petitioner was allowed to use its own methods in meeting both its general contractual obligations (see, Exhibit "1," p. 52, article V) as well as its obligation to provide guard services. Under the contract, petitioner was responsible for placing and maintaining the necessary guards on the site (see, Exhibit "1," p. 84, article XXXIX, and p. 185, Item 1 § 1.1). Although Mr. Edward Plotkin, petitioner's project manager, testified that during the project the guards were sometimes positioned by a representative of the City, this testimony, in itself, does not demonstrate a sufficient level of control to support a finding of agency (see, Matter of Sea-Land Restoration, supra). Further, petitioner was responsible for any injury, defacement or theft of the property of the City regardless of whether it was petitioner's fault or not (see, Exhibit "1," p. 83, article XXXVI; p. 180 § 57), and petitioner was not reimbursed for the retention of a supervising security guard, as this service was considered overhead by the contract (see, Exhibit "1," p. 186, Item 1 § 1.4).

Third, there is no evidence that petitioner held itself out as an agent for the City of New York when making arrangements with the guard service (cf., Kern-Limerick, Inc. v. Scurlock, supra), nor that petitioner provided the guard service with governmental purchase orders or exemption documents (see, 20 NYCRR 529.2[b][2]). Further, petitioner did not submit any bills

or other documents from the guard services indicating that the guard services considered petitioner to be the purchaser on behalf of New York City.

Petitioner has offered a memorandum from the Assistant Commissioner and Director of Water Supply of the Department of Environmental Protection to the General Counsel of that Department as proof of the agency relationship. The document, dated January 17, 1989, states, in part:

> "The State has informed the Contractor [petitioner] that DEP's legal department should formally notify the State that the armed guard service was ordered by the City via the subject change order and that the Contractor is an agent for the City.
>
> * * *
>
> "Since this service was ordered by the DEP (City), since the City is an exempt organization, and since the Contractor is an agent for the City on the change order the subject sales tax should be waived" (Exhibit "5").

The document was offered to demonstrate that, from the City's point of view, petitioner was acting as an agent of the City for the purpose of securing guard services (Hearing Tr., p. 84). We conclude that this memorandum, written long after the execution of the contract, cannot establish an agency relationship that is not evidenced by the contract.

In sum, the contract and the circumstances surrounding it fail to support a finding of agency. Therefore, the guard services are subject to tax.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is granted;
2. The determination of the Administrative Law Judge is reversed;
3. The petitions of MGK Constructors are denied; and

4. The notices of determination and demand and the notices and demand are sustained.

DATED: Troy, New York
March 5, 1992

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

/s/Maria T. Jones
Maria T. Jones
Commissioner