

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition :
of :
KEYBOARD() ALPHA WINDOW SYSTEMS, LTD. :
: :
KEYBOARD() 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 September 1, 1989 through May 31, 1993. :
:

In the Matter of the Petition :
of :
KEYBOARD() GARY LEWIS, OFFICER :
DECISION :
KEYBOARD() for Revision of a Determination DTA Nos. 813355, :
or for Refund of Sales 813356, 813357, :
and Use Taxes under Articles 28 and 29 AND 813358 :
of the Tax Law for the Period September :
1, 1989 through May 31, 1993. :
:

In the Matter of the Petition :
of :
KEYBOARD() JAMES BAKER, OFFICER :
: :
KEYBOARD() 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 September 1, 1989 :
through May 31, 1993. :
:

In the Matter of the Petition :
of :

KEYBOARD()PETER POULIKIDIS, OFFICER

KEYBOARD()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 September 1, 1989
through May 31, 1993.

KEYBOARD()Petitioners Alpha Window Systems, Ltd., 1760 Fifth Avenue, Bay Shore, New York 11706-1739; Gary Lewis, Officer, 37 Shinebone Lane, Commack, New York 11725-5510; James Baker, Officer, P.O. Box 24, St. James, New York 11780-0024 and Peter Poulikidis, Officer, 3133 Enos Street, Bellmore, New York 11710-5318, filed an exception to the determination of theKEYBOARD(enter alj name) Administrative Law Judge issued on August 15, 1996. Petitioners appeared by Louis F. Brush, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Kathleen D. Church, Esq., of counsel).

Petitioners did not file a brief on exception. The Division of Taxation filed a letter in lieu of a brief in opposition. Oral argument was not requested.

Commissioner DeWitt delivered the decision of the Tax Appeals Tribunal. Commissioners Jenkins and Pinto concur.

Issue

Whether the Division of Taxation properly determined additional sales and use taxes due from Alpha Window Systems, Ltd. for the period at issue.

Findings of Fact

We find the facts as determined by the Administrative Law Judge except for findings of fact "20" through "26" which have been deleted as irrelevant to the rendering of this decision. These facts are set forth below.

Petitioner Alpha Window Systems, Ltd. ("Alpha Window Systems") is a manufacturer of windows. Petitioners did not present a witness to provide details concerning the nature of the business of Alpha Window Systems. Neither did any of the individual petitioners appear at the hearing to testify. Rather, it is necessary to review the audit report and tax returns, which were introduced into evidence by the Division of Taxation ("Division"), in order to make factual findings concerning the company's operations.

Alpha Window Systems was a Long Island-based manufacturer of windows. According to an entry dated December 1, 1992 in the auditor's log, which is included in the Division's Exhibit "M",

Michael Sheehan, CPA, the company's accountant at the time of the audit in 1992, informed the auditor that Alpha Window Systems did not sell windows to contractors but rather installed all of the windows which it manufactured. However, it is observed that in the narrative section of the audit report (page 10 of Exhibit "M"), the auditor noted to the contrary that when she visited one of the showrooms of Alpha Window Systems, an unspecified employee indicated that windows were also sold without installation. This narrative section also noted that at the time of the audit, Alpha Window Systems maintained three showrooms, all located on Long Island in Merrick, Selden and Bay Shore. A fourth showroom in Carle Place, according to the narrative, was closed in January 1992.

Included in the Division's Exhibit "M" (at p. E 78) is a photocopy of an advertisement of Alpha Window Systems which appeared in the Long Island newspaper, Newsday, on July 6, 1993. In this advertisement, the vendor is described as "Alpha Window Factory, Long Island's Window" and offered a free air conditioner with the purchase of "Alpha bays, sliders, bows, casements, double hungs, picture windows, sliding glass doors". Fine print at the bottom of the ad noted that for a free air conditioner, the minimum purchase was "7 Alpha Windows or 1 bay or bow window". The advertisement also offered immediate installation, low cost financing and "no-obligation in-home design consultation". In addition, the advertisement noted "special savings on all styles" of vinyl siding.

A photocopy of a standard sales contract apparently used by Alpha Window Systems as a contractor with its customers, which is also included in the Division's Exhibit "M" at an unpaginated page following the photocopy of the advertisement, provides in relevant part as follows:

"By this agreement, Contractor agrees to sell and Customer agrees to buy the services and materials set forth in the Work and Materials Description below UPON THE TERMS AND CONDITIONS SET FORTH ON THE FRONT AND REVERSE SIDE HEREOF. There are NO EXTRAS, SPECIAL INSTRUCTIONS OR SPECIFICATIONS unless specifically set forth below. See note* below".

The note referred to above provided as follows:

"Prices include complete removal of old sashes and clean up. Moldings and frames are not changed unless specified in Additional Remarks below. Air conditioners are the customer's responsibility to remove and replace. Customer is responsible to remove and replace all drapes, curtains, blinds and shutters."

A review of the photocopies of the Federal income tax returns of Alpha Window Systems, a subchapter S corporation, for 1990 and 1991, also included in the Division's Exhibit M, described the corporation's business activity as "manufacturing" and its product or service as "replace windows". The corporation reported total income before deductions of \$3,031,456.00 and \$2,620,150.00, for 1990 and 1991, respectively, calculated as follows:

	1990
1991	
Gross receipts or sales	\$6,511,992.00
\$5,384,575.00	
Less: Cost of goods sold	<u>3,483,261.00</u>
<u>2,778,566.00</u>	
Gross profit	\$3,028,731.00
\$2,606,009.00	

Miscellaneous Income	<u>2,724.00</u>
<u>14,141.00</u>	
Total income	\$3,031,456.00
\$2,620,150.00	

It is further observed that these tax returns disclose deductions for "salaries and wages" of \$253,961.00 and \$306,204.00 for 1990 and 1991, respectively, as well as deductions for so-called "contract labor" of \$865,894.00 and \$750,732.00 for 1990 and 1991, respectively, and compensation of officers of \$370,403.00 and \$369,000.00 for 1990 and 1991, respectively. It is noted that the corporation reported ordinary losses, after deductions, of \$723,994.00 and \$351,262.00 for 1990 and 1991, respectively.

In addition, the Federal tax returns provide some information about the individual petitioners in respective statements designated "Statement 1, Compensation of Officers". These statements disclose that Peter Poulikidis, Gary Lewis and James Baker each own 33.333% of the corporation's stock, each devoted 100% of their time to Alpha Window Systems, and each received the same compensation of \$123,000.00 in 1990 and of \$123,470.00, \$123,473.00 and \$123,460.00, respectively, in 1991. It is observed that the individual petitioners withdrew their respective challenges to the Division's determination that they as individuals were persons responsible for the collection of sales and use taxes on behalf of Alpha Window Systems. As a result, the record does not include any details concerning the specific duties and responsibilities of the individual petitioners in relation to the corporation.

Included in the Division's Exhibit "M" (at p. E 53) is a transcription of the sales and use tax returns filed by Alpha Window Systems during the period at issue. The company reported minimal taxable sales as follows:

Quarter Tax Paid Ending	Gross Sales	Taxable Sales	Purchases Subject To Use Tax
11/30/89 \$ 2,308.07	\$ 189,520.00	\$ 29,986.00	-0-
2/28/90 682.85	1,209,174.00	8,648.00	-0-
5/31/90 271.76	1,799,502.00	3,551.00	-0-
8/31/90 88.77	1,746,477.00	1,151.00	-0-
11/30/90 784.58	1,993,339.00	10,317.00	-0-
2/28/91 61.85	727,737.00	802.00	-0-
5/31/91 73.24	1,171,610.00	930.00	-0-
8/31/91	1,240,082.00	596.00	12,073.00

953.14			
11/30/91	1,790,198.00	2,322.00	13,616.00
1,277.83			
2/29/92	701,760.00	2,118.00	-0-
176.20			
5/31/92	903,204.00	1,595.00	-0-
129.67			
8/31/92	849,089.00	749.00	-0-
62.87			
11/30/92	1,158,177.00	17,456.00	-0-
1,483.35			
2/28/93	582,452.00	1,501.00	-0-
127.67			
5/31/93	<u>843,589.00</u>	<u>2,779.00</u>	
-0-		<u>236.55</u>	
Totals	\$16,905,910.00	\$84,501.00	\$25,689.00
\$8,718.40			

The fact that Alpha Window Systems reported gross sales of nearly \$17,000,000.00 during the audit period while reporting sales and use tax due of an amount less than \$9,000.00, apparently prompted the Division to audit the company's returns.

The Audit

Alpha Window Systems did not cooperate during the audit. The auditor's log shows that an appointment letter dated August 27, 1992 was sent to Alpha Window Systems scheduling the initial appointment to commence the audit on September 24, 1992. The log indicated that the company cancelled five succeeding appointments for September 24, 1992, November 10, 1992, November 17, 1992, May 4, 1993 and June 3, 1993. Frustrated, the auditor then sent a certified letter requesting the books and records of Alpha Window Systems in order to conduct her audit of the company's sales and use tax returns. The audit report indicates that the company failed to make the following records available: sales journal, cash receipts journal, sales invoices (test period), purchase journal, check disbursements journal, purchase invoices (test period), contractor's job cost book or sheets, exemption certificates (including resale certificates, exempt organization certificates, capital improvement certificates, exempt use certificates, contractor exempt purchase certificates), disposition of assets details, adjusting entries and lease contracts.

Consequently, the Division issued a Statement of Proposed Audit Adjustment dated July 1, 1993 against Alpha Window Systems asserting tax due for the audit period of \$1,483,048.58 plus penalty and interest. Additional tax due of \$1,442,178.99 was computed based upon additional taxable sales of \$18,654,822.97, which represented the amount of gross sales taken from the corporation's sales tax returns and federal income tax returns. The Division had disallowed all non-taxable sales claimed by Alpha Window Systems. The auditor described her methodology as

follows:

"[W]e pick up all the gross sales that appear in the federal, we divided it by month, and for the amount that we don't have in the federal, we take the amount that they put it in the sales tax returns like a gross sales. And for the last three months we projected because we can't have any information. And was based in the report December to February before" (tr., p. 76).

Additional tax due of \$40,869.58 was based upon the corporation's acquisition and disposal of fixed assets because no documentation was provided to show that sales tax had been paid on such transactions. It appears that such transactions related to the closing of one of Alpha Window System's showrooms, which occurred during the audit period.

On August 5, 1993, about a month after the issuance of the Statement of Proposed Audit Adjustment dated July 1, 1993, the Division received a power of attorney from Louis F. Brush, Esq., authorizing his representation. The auditor's narrative, included in the audit report at page 10 of 11 pages of the Division's Exhibit "M", noted the continued lack of cooperation on the part of petitioners:

"We contacted him, and asked for the books and records. He said that he will get in contact with the vendor and he will give us a call back. He never did, I left several messages with his secretary, but we did not receive any response. We uploaded the case as not agreed and with no payment."

The Division then issued a Notice of Determination dated October 18, 1993 against Alpha Window Systems asserting tax due of \$1,483,048.58 plus penalty and interest. Corresponding notices also dated October 18, 1993 were issued by the Division against Gary Lewis, James Baker and Peter Poulikidis, respectively, as officers of the corporate petitioner, which also asserted sales tax due of \$1,483,048.58 plus penalty and interest. As noted above, petitioners have conceded that the individual petitioners were each persons required to collect sales tax on behalf of the corporation.

Approximately six months after the issuance of the Notice of Determination dated October 18, 1993, a conciliation conference was conducted at petitioners' request on April 11, 1994. Six months after the conciliation conference, by conciliation orders dated October 7, 1994, the amount of tax asserted due against each of the petitioners was reduced by \$1,155,018.70, from the \$1,483,048.58 asserted in the notices of determination dated October 18, 1993 to \$328,029.88 plus penalty and interest as recomputed by the conciliation orders.

Much of the hearing in this matter was taken up by questioning of the auditor concerning this recomputation of tax due. It is initially observed that the auditor, in attempting to recompute tax due, again faced a lack of cooperation. In a document marked into evidence as the Division's Exhibit "O", the auditor summarized the continued lack of cooperation in producing necessary records. An appointment scheduled for May 16, 1994 was cancelled by petitioners' representative. On May 17, 1994, the auditor went to the representative's office, but no invoices were available for her review. An appointment for the following day, May 18, 1994, was cancelled by petitioners' representative. The auditor placed three phone calls on June 2, June 6, and June 7, 1994 attempting to make another appointment to review records. On June 13, 1994, the auditor returned the phone call of petitioners' representative of June 9, 1994, and the auditor's notes state that the representative "offer[ed] us a sample". An appointment was set for June 28, 1994, but the petitioners' representative cancelled once again, and the appointment was rescheduled for July 8, 1994. However, on July 7, 1994, petitioners' representative left a message for the auditor cancelling the appointment for July 8, 1994. The auditor contacted the conferee who scheduled an appointment for her to review records on July 21, 1994. On July 21, 1994, the auditor's notes state that "only invoices for raw materials were available", and that she gave petitioners' representative to July 28, 1994 "to get the rest of [the] documentation". After several additional phone calls to petitioners' representative, the auditor finally reached the representative, who informed her that "there were no more invoices". On August 16, 1994, the conferee advised the auditor to "work with the information available".

Despite the frustrations encountered by the auditor in her attempt to recompute tax asserted due, she nonetheless revised her audit. Originally, as noted above, the auditor treated as taxable all of Alpha Window Systems' sales which resulted in an assessment in excess of a million dollars. Following the conciliation conference, the auditor accepted the corporation's nontaxable sales, and her focus shifted to determining whether the corporation paid sales tax on its purchases. According to the auditor, if the corporation did not pay sales tax on its purchases, then use tax was due. The auditor closely examined the purchase invoices of Alpha Window Systems for a three month period, March through May of 1991. The auditor selected this particular test period. If there was no designation of sales tax on a particular purchase invoice or if an invoice was missing, the auditor concluded that tax had not been paid. She determined that sales tax had not been paid on purchases of \$225,768.79 out of purchases tested of \$296,064.58, resulting in a margin of error of 76.2566%.

The auditor's recalculation of tax due was marked into evidence as the Division's Exhibit "N", and on page 4 of this document, a schedule shows the application of this margin of

error of 76.2566% to the purchases of Alpha Window Systems during the audit period as follows:

Period Tax due Ending	<u>Purchases</u>	76.2566% of <u>purchases</u>
Nov. '89	\$544,394.95	\$415,137.08
\$31,135.28		
Feb. '90	544,394.95	415,137.08
31,135.28		
May '90	544,394.95	415,137.08
31,135.28		
Aug. '90	544,394.95	415,137.08
31,135.28		
Nov. '90	544,394.95	415,137.08
31,135.28		
Feb. '91	370,007.14	282,154.86
21,161.61		
May '91	282,813.23	215,663.75
16,174.78		
Aug. '91	282,813.23	215,663.75
16,174.78		
Nov. '91	282,813.23	215,553.75
17,253.10		
Feb. '92	250,448.92	190,983.83
15,278.71		
May '92	234,266.77	178,643.87
14,291.51		
Aug. '92	234,266.77	178,643.87
14,291.51		
Nov. '92	234,266.77	178,643.87
15,184.73		
Feb. '93	234,266.77	178,643.87
15,184.73		
May '93	<u>234,266.77</u>	<u>178,643.87</u>
<u>15,184.73</u>		
Totals	\$5,362,204.32	\$4,089,034.70
\$315,856.60		

The auditor testified that in revising the tax asserted due, she utilized the general ledger of Alpha Window Systems for the amounts of raw material purchased as specified in an account known as "inventory-raw materials". The auditor noted that the amount shown in the general ledger for "inventory-raw materials" was not the same as the amount shown on the federal tax return for purchases. Her request for "the adjusting entry" which would reconcile the two went unanswered (tr., p. 171). Further, because petitioners did not provide the general ledger information for 1989 and 1993, the auditor projected amounts. For 1989, she divided the amount of purchases for 1990 by 12 to obtain a monthly amount for purchases. She then multiplied that monthly amount by four to determine the amount of purchases for the four month period in 1989. Similarly, for 1993, the auditor divided the amount of purchases for 1992 by 12 to obtain a

monthly amount for purchases. She then multiplied that monthly amount by five to determine the amount of purchases for the five month period in 1993 included in the audit period.

It is observed that the Division's Exhibit "P" is a photocopy of pages from the general ledger of Alpha Window Systems for the months of March, April and May 1991 on which the auditor specifically marked the particular purchases where tax had been paid. Purchases where tax had not been paid according to the auditor can easily be determined. Consequently, the record is clear which purchases are at issue. It is noted that petitioners have introduced no evidence from any of the entities from which the corporation purchased materials to challenge the auditor's determination that no tax was paid on such purchases.

The auditor also reduced tax asserted due based upon the corporation's acquisition and disposal of fixed assets from \$40,869.58, as noted above to \$12,173.29, as noted on the first page of Exhibit "N" where the auditor noted that such reduction resulted from "additional information provided". This reduced amount of \$12,173.29 plus the \$315,856.60, calculated as due on purchases, equals \$328,029.89, one cent more than the amount specified in the conciliation order dated October 7, 1994, as noted above.

The hearing in this matter was continued to conclusion on September 18, 1995 approximately two months after it had been commenced on July 5, 1995. In that interval, petitioners provided the auditor with Alpha Window System's "1991 invoices with a printout by vendor name by quarter" (tr., p. 205). The computer printout by vendor name by quarter was marked into evidence as petitioners' Exhibit "26". Petitioners did not present a witness to identify this document but rather relied on the auditor to give her opinion concerning the nature of this document which she described as a record of the corporation's accounts payable. The auditor testified that she compared invoices, included in petitioners' Exhibits "27" and "28", to this document and redid her test by also including an analysis of the month of September 1991. The auditor testified that when she reexamined the invoices for the months of March, April, and May 1991, by comparing them to this accounts payable record, there was an increase in the margin of error to the disadvantage of petitioners (tr., p. 282). However, she apparently relied upon her earlier calculation of a margin of error for this three month test period, and the Division's Exhibit "U" shows a summary of the auditor's revised test which resulted in a slight decrease in the margin of error used by her of 76.2566% to a rounded 74% because of a lesser margin of error of a rounded 71% calculated for the month of September 1991. Applying this reduced margin of error to the purchases of Alpha Window Systems resulted in a reduction of tax due on purchases from \$315,856.60 as indicated above to \$307,520.65. Since tax due on fixed assets remained \$12,173.29, the further revised amount of total tax asserted due is \$319,693.94, which is a further reduction of

the amount shown due in the conciliation order of \$328,029.88.

Petitioners' Presentation

Petitioners' case primarily consisted of the cross-examination of the auditor. Petitioners' only witness was the corporation's purchasing agent, Beth Baker, a sister-in-law of petitioner James Baker. She testified that she was responsible for the purchase of all materials for the corporation's manufacturing of windows. She offered no testimony concerning the corporation's practice of paying or not paying sales tax on such purchases. Rather, she merely noted that the corporation relied upon its former accountant, Michael Sheehan, "as to what is the correct amount of tax to be paid" in responding "Yes" to a leading question (tr., p. 293). Further, it is noted that petitioners introduced no evidence from the vendors who sold Alpha Window Systems its raw materials concerning their collection of sales tax on the sale of such raw materials.

Opinion

In his determination, the Administrative Law Judge reviewed the standards concerning the burden of proof in matters before the Division of Tax Appeals. He noted that a determination of tax must have a rational basis in order to be sustained upon review and the presumption of correctness raised by the issuance of the assessment, in itself, provides the rational basis, so long as no evidence is introduced challenging the assessment. He further noted that the Division does not have the burden to demonstrate the propriety of its assessment and that petitioners have a heavy burden to prove the assessment erroneous. The Administrative Law Judge concluded that a determination of whether there was a rational basis for the assessments at issue was dependent on what was known by the auditor at the time the notices were issued. Since petitioners failed to provide adequate books and records for the auditor's review after repeated attempts by the auditor to obtain their cooperation, the Administrative Law Judge concluded that the auditor was justified in deeming all gross sales by the corporation to be taxable and imposing additional tax on the corporation's acquisition and disposal of fixed assets. Further, the Administrative Law Judge disagreed with petitioners' argument that the burden of proof shifted to the Division to prove that the amount of additional tax asserted due was correct when the basis for such additional taxes changed as a result of the conciliation conference. The Administrative Law Judge stated that:

"there is no basis in statute and no cases have been cited by petitioners to support the shifting of the burden of proof to the Division in the circumstances at hand. It is further noted that petitioners have not been prejudiced in any fashion by the recalculation of tax due based

upon the auditor's analysis of the corporation's purchases which resulted in a substantial reduction in tax asserted due since they have been given many opportunities to present documentation to show that tax had been properly paid on such purchases (cf., Matter of Chuckrow, Tax Appeals Tribunal, July 1, 1993). Under Tax Law § 1133(b), Alpha Window Systems was properly treated as liable for sales tax which it, as a customer, failed to pay to its vendors (cf., Matter of Gartner Group, Inc., Tax Appeals Tribunal, December 8, 1994). In sum, petitioners have not shouldered their burden of proving that they are entitled to any further reduction of the amount of taxes asserted due" (Determination, conclusion of law "D").

Finally, the Administrative Law Judge concluded that petitioners were not entitled to an exemption from use tax for out-of-state material purchases incorporated into real property located in the State (Tax Law § 1118[2]).

On exception, petitioners assert the same arguments which they made to the Administrative Law Judge. They state that since the auditor determined petitioners' tax liability on "grounds not stated in the original Notice of Deficiency [sic]" the burden of proof shifted to the Division to demonstrate the propriety of its assessment. Further, petitioners assert that the purchases by the petitioner corporation on which the tax assessment was based were nontaxable events because they were out-of-state purchases of the component parts of a product produced for sale and sold in the ordinary course of business.

In opposition, the Division argues that the arguments of petitioners were considered by the Administrative Law Judge and were correctly found by him to be unavailing. Accordingly, the Administrative Law Judge's determination should be affirmed.

Petitioners offer no authority to support their arguments on exception nor do we find any support in the facts or the law for these arguments. The issues raised by petitioners were each presented to and considered by the Administrative Law Judge. After reviewing all the evidence presented in this case, we find that the Administrative Law Judge correctly and adequately addressed these issues and we affirm his determination for the reasons stated therein.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Alpha Window Systems, Ltd.; Gary Lewis, Officer; James Baker, Officer; and Peter Poulikidis, Officer is denied;

2. The determination of the Administrative Law Judge is

affirmed;

3. The petitions of Alpha Window Systems, Ltd.; Gary Lewis, Officer; James Baker, Officer; and Peter Poulikidis, Officer are denied; and

4. The notices of determination dated October 18, 1993, as modified by the auditor plus penalty and interest, are sustained.

DATED: Troy, New York
May 1, 1997

DeWitt

/s/Donald C.

Donald C. DeWitt
President

Jenkins

/s/Carroll R.

Carroll R. Jenkins
Commissioner

Jr.

/s/Joseph W. Pinto,

Joseph W. Pinto, Jr.
Commissioner