STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petitions	:	
of	:	
AERO SERVICES INTERNATIONAL, INC.	:	DECISION
for Redetermination of Deficiencies or for Refund of Tax on Petroleum Businesses under Article 13-A of the Tax Law for the Period September 1, 1991 through November 30, 1993.	:	DTA NOS. 817801 817802, 817803, 817804 817805, 817806, 817807 AND 817808

Petitioner Aero Services International, Inc., 660 Newtown-Yardley Road, Newtown, Pennsylvania 18940, filed an exception to the determination of the Administrative Law Judge issued on November 8, 2001. Petitioner appeared by Stevens & Lee (Christopher M. Cicconi, Esq., of counsel) and Stroock & Stroock & Lavan, LLP (Robert Abrams, Esq. and Joel Cohen, Esq., of counsel). The Division of Taxation appeared by Barbara G. Billet, Esq. (John E. Matthews, Esq., of counsel).

Petitioner filed a brief in support of its exception. The Division of Taxation did not file a brief in opposition. Oral argument, at petitioner's request, was heard on March 13, 2002 in New York, New York.

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

ISSUES

I. Whether petitioner is subject to additional tax due on petroleum businesses pursuant to Article 13-A of the Tax Law.

II. Whether the statute giving rise to petitioner's asserted Article 13-A liability is either facially unconstitutional or unconstitutional as applied to petitioner's circumstances.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

During the audit period petitioner was registered with the Department of Taxation and Finance as a fixed base operator ("FBO") and was engaged in the sale of kero-jet fuel from its business location at the Westchester County Airport in White Plains, New York ("New York FBO").

From the late 1940s through the mid 1980s petitioner prospered in its operation of 20 FBOs, including the New York FBO, which were located in various parts of the United States. The on-site management at these locations generally operated these facilities with a great deal of autonomy from petitioner's corporate headquarters located in Newtown, Pennsylvania.

An Article 13-A petroleum business tax audit of petitioner's New York FBO was commenced in September 1994, by the issuance of an appointment letter from the Division's Capital Region District Office. The appointment letter included a request for all relevant books and records including exemption and resale certificates. Further, such requests for relevant books and records were made by the auditor during the course of the audit and during field visits. All records produced by petitioner were examined. The records produced by petitioner included

copies of tax returns, purchase invoices, computerized sales reports, credit card receipts and fuel cost forms. Of these records, the fuel cost forms were obtained from the New York FBO and the remaining records came from petitioner's Newtown, Pennsylvania corporate headquarters. No exemption or resale certificates were provided to the Division at any time during the audit.

The Division's auditor examined petitioner's petroleum business tax ("PBT") returns for the audit period (Forms PT-200, PT-202 and supporting schedules). This examination revealed that all gallons of kero-jet fuel sold during the audit period were reported on line 8 of each Form PT-202 as "[s]ales to persons registered as aviation fuel businesses or under 12A or to United States government, New York State and its municipalities, or consumed by you in your aircraft." On line 13 of each Form PT-202 petitioner reported that none of the gallons of kero-jet fuel were consumed by petitioner in its own aircraft. On the PBT returns for each quarter at issue petitioner reported no taxable sales and paid only the minimum petroleum business tax of $75.00 per quarter. Petitioner's total reported volume of nontaxable sales for the audit period was 5,844,662 gallons. Nine notices of determination were issued to petitioner. Relevant portions of the schedule of sales by quarter with associated tax, penalty and interest due are reproduced below.

Notice #	q/e Date	Gallons	Tax rate	Tax paid	Add'l tax due	Penalty	Interest	Total
41213PP01	11/30/91	638,208	0.1277	$75.00	$81,424.16	$79,723.98	$78,023.80	$239,171.94
50307PP01	02/29/92	575,281	0.1277	75.00	73,388.38	70,202.20	67,016.01	210,606.59
50602PP01	05/31/92	640,879	0.1484	75.00	95,031.44	89,037.51	83,043.57	267,112.52
50912PP01	08/31/92	643,011	0.1484	75.00	95,347.83	87,550.87	79,753.91	262,652.61
51212PP01	11/30/92	738,338	0.1484	75.00	109,494.36	98,720.20	87,946.04	296,160.60
60301PP01	02/28/93	590,261	0.1484	75.00	87,519.73	77,557.72	67,595.71	232,673.16
60612PP01	05/31/93	711,354	0.1484	75.00	105,489.93	91,847.68	78,205.43	275,543.04
60904PP01	08/31/93	696,730	0.1484	75.00	103,319.73	88,385.01	73,450.28	265,155.02
61213PP01	11/30/93	610,600	0.1484	75.00	90,538.04	76,111.01	61,684.12	228,333.24
Totals		**5,844,662**		**$675.00**	**$841,553.60**	**$759,136.24**	**$676,718.87**	**$2,277,408.71**

The on-site manager of the New York FBO used internal pricing sheets ("fuel cost forms") to determine the price he would charge for fuel. The manager reviewed such completed fuel cost forms with the vice president responsible for oversight of the New York FBO who, during the audit period, was located in Houston, Texas. The fuel cost forms were not submitted to petitioner's headquarters in Newtown. The vice president in Houston simply provided the accounting department in Newtown with summaries of the fuel cost forms detailing the total sales price and selling volume for the New York FBO. These summaries were utilized by the accounting department to prepare and file the petroleum business tax returns at issue herein.

The auditor verified the retail selling price for each quarter by reference to petitioner's quarterly sales reports.

Petitioner purchased the fuel at issue from Exxon Company, USA, paying to Exxon the base price for the fuel plus Federal excise tax, New York State prepaid sales tax and an airport fee.

Coopers & Lybrand was petitioner's public accounting firm for the audit period. As part of its annual audit for petitioner, a copy of the report of which was filed each year as a public record with the U.S. Securities and Exchange Commission, Coopers & Lybrand would send a state tax expert to petitioner's headquarters in Newtown for several days each year to review petitioner's performance and records for compliance with state tax statutes and regulations including the petroleum business tax. Petitioner's management was never advised by Coopers & Lybrand of any failure to comply with any of New York's tax laws.

On May 20, 1994, subsequent to the sale of the New York FBO and four months prior to the initiation of the Division's audit, the current management team was put in place when Triton Energy Corporation, petitioner's principal shareholder, concluded the sale of its interests in

petitioner to Transtech Holding Co., Inc. Since the Coopers & Lybrand audits of petitioner never disclosed any unpaid New York taxes, Transtech was unaware that any such liability existed at the time it purchased Triton's holdings in petitioner.

The parties have stipulated that in the event the Division is unable to meet its burden to prove its entitlement to fraud penalty, then the Division will bear the burden to prove the absence of reasonable cause in order to sustain the penalty for failure to pay imposed by Tax Law § 289-b(1)(a).

The fuel cost forms provided to the Division revealed that the retail selling price of each gallon of kero-jet fuel included the Article 13-A gross receipts tax as a separate line item.

The kero-jet fuel sold by petitioner to its customers and pumped by it into the fuel tanks of its customers' aircraft was, prior to the sale, removed from storage facilities at the Westchester County Airport owned by Exxon Company USA or petitioner.

A narrative report prepared by Division audit personnel referenced the statement of Wally Sipe, who formerly served as the general manager of the New York FBO and whose duties included the preparation of the fuel pricing sheets. Mr. Sipe's statement, as recounted in the narrative report, reads, "that the home office was aware of the Tax Law and that all sells [sic] were taxable."

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge found that petitioner was a registered New York State Fixed Base Operator engaged in the sale of kero-jet fuel during the period in issue. For the nine quarters under review, petitioner claimed to have made no taxable sales of kero-jet fuel and that all sales were exempt. However, petitioner produced no exempt transaction certificates or other evidence

to support this claim. In fact, petitioner treated all its sales as taxable and collected $842,228.60 in petroleum business tax and paid over to the Division only $675.00, retaining the balance of $841,553.60 for its own use. Although petitioner tried to lay the blame for these failures on its accountants and poor intra-company communications, the Administrative Law Judge found that internal pricing sheets showing tax being collected in the selling price were withheld by the on-site managers from the Pennsylvania headquarters and the public accounting firm which audited petitioner's operations. Also lending weight to this conclusion was the testimony of a manager that the selling price included the petroleum business tax and that management was aware of it.

Given this underlying proof of consistent and substantial understatements of taxable sales for the periods in issue, coupled with incomplete and inaccurate records, and the fact that petitioner did not provide its accounting department with complete and accurate information for the preparation and filing of accurate petroleum business tax returns, the Administrative Law Judge sustained the Division of Audit's imposition of fraud penalty (***Merritt v. Commissioner***, 301 F2d 484, 62-1 USTC ¶ 9408; ***Matter of Cousins Serv. Sta.***, Tax Appeals Tribunal, August 11, 1988; ***Matter of Sener***, Tax Appeals Tribunal, May 6, 1988).

The Administrative Law Judge rejected petitioner's facial challenge to Tax Law § 301-a(a)[1] given the lack of jurisdiction to make such a determination by the Division of Tax Appeals (***Matter of Unger***, Tax Appeals Tribunal, March 24, 1994). In considering petitioner's argument that the statute is unconstitutional as applied to petitioner's unique circumstances, the Administrative Law Judge noted that petitioner did not demonstrate that Tax Law § former 301-

[1]Because the audit period began on September 1, 1991 and Tax Law § 301(a)(1)(iii) (the section challenged by petitioner) was not in force after August 31, 1990, the reference should be to Tax Law § 301-a(a) which became effective on September 1, 1990 (***see***, L 1990, ch 190, § 216).

a(a) impermissibly discriminates solely as applied to petitioner; rather, the argument applies to all entities subject to the tax who are engaged in interstate commerce and, thus, the challenge is to the facial constitutionality of the statute. As stated above, consideration of such issues is beyond the jurisdiction of the Tax Appeals Tribunal (***Matter of Texas Eastern Transmission Corp.***, Tax Appeals Tribunal, November 12, 1998, ***confirmed Matter of Texas Eastern Transmission Corp. v. Tax Appeals Tribunal***, 260 AD2d 127, 699 NYS2d 560, ***affd*** 95 NY2d 323, 717 NYS2d 69).

ARGUMENTS ON EXCEPTION

Petitioner has abandoned its challenge to the constitutionality of the imposition of tax pursuant to Tax Law § 301-a(a). However, it believes it should not be held liable for the actions of prior management which it inherited as a result of a change in control of the company in 1994. That being said, petitioner then asserts that the Division did not meet its burden of establishing willful, knowledgeable or intentional conduct sufficient to support the imposition of the fraud penalty. Petitioner contends that the sheer size and complexity of the corporation, its poor communications and reliance on its auditors were its only mistakes. Further, it argues that the double hearsay statement of Mr. Sipes, petitioner's own manager, at the Westchester Airport was not sufficient to confer intent to defraud on the company. In sum, petitioner believes it committed only "simple error" and has not engaged in the type of conduct which constitutes fraudulent behavior.

OPINION

The Administrative Law Judge has fully and correctly addressed each of the issues raised by petitioner. Thus, we affirm the determination of the Administrative Law Judge for the reasons

stated therein. Petitioner has offered no evidence below or any arguments before us which would justify modifying the determination of the Administrative Law Judge in any respect.

In response to petitioner's arguments to this Tribunal, we conclude that the change in management had no effect on the transactions which took place during the audit period or the company's continued liability for the taxes due and owing to the State of New York. It is of no moment that the current management team is without fault; rather, the corporate entity for which that management team is responsible has a continuing duty to properly collect, report and remit the taxes due and owing. In this matter, petitioner failed to maintain records which would have established its right to an exemption from tax (a position never even mentioned in petitioner's exception or brief). It consistently and substantially understated the tax throughout the audit period on its returns while actually collecting it. It generated internal memoranda (e.g., fuel cost forms) which indicated tax was being collected and separately stated as a line item, but failed to inform its auditors of this breakdown. Petitioner now claims this was all "simple error" caused by an internal communications breakdown and poor representation and advice by its public accounting firm.

We must reject these arguments as a mischaracterization of the circumstances. Fraud may be proven by circumstantial evidence, including a taxpayer's course of conduct (***Intersimone v. Commissioner***, T.C. Memo 1987-290, 53 TCM 1073; ***Korecky v. Commissioner***, 781 F2d 1566, 86-1 USTC ¶ 9232). In this case, the Administrative Law Judge's analysis of the evidence demonstrated that petitioner willfully, knowingly and intentionally underreported and underpaid the petroleum business taxes due and owing. Although substantial underreporting alone is not enough to establish fraud, where it continues for nine quarters there is strong evidence of fraud

(***Merritt v. Commissioner***, ***supra***; ***Matter of Cousins Serv. Sta.***, ***supra***). Additional indicia of an intention to evade tax can be found in the fuel cost forms, the failure to maintain adequate books and records and the statement of petitioner's manager, Mr. Sipes, given to a Division investigator (***Intersimone v. Commissioner***, ***supra***). On this basis, we believe the evidence, considered as a whole, supports the Administrative Law Judge's determination to uphold the imposition of fraud penalty by the Division of Taxation.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Aero Services International, Inc. is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petitions of Aero Services International, Inc. are denied; and

4. The nine notices of determination are, in all respects, sustained.

DATED: Troy, New York
September 12, 2002

/s/Donald C. DeWitt
Donald C. DeWitt
President

/s/Carroll R. Jenkins
Carroll R. Jenkins
Commissioner

/s/Joseph W. Pinto, Jr.
Joseph W. Pinto, Jr.
Commissioner