

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition :
of :
MICHAEL CONSTANTINI : DECISION
 : DTA NO. 820590
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 June 1, 2001 through February 28, 2004. :

Petitioner, Michael Constantini, filed an exception to the determination of the Administrative Law Judge issued on February 1, 2007. Petitioner appeared *pro se*. The Division of Taxation appeared by Daniel Smirlock, Esq. (Lori P. Antolick, Esq., of counsel).

Petitioner filed a brief in support of his exception and the Division of Taxation filed a brief in opposition. Petitioner filed a reply brief. Oral argument was not requested.

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

ISSUE

Whether the Division of Taxation properly determined additional sales tax due from petitioner as an officer or responsible person of Nature Health Food Gourmet Corporation.

FINDINGS OF FACT

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

Petitioner, Michael Constantini, was president of Natural Health Food Gourmet Corporation ("Natural Health"), which operated a restaurant and pizzeria located at 124 West

72nd Street, New York, New York. The business operation used cash registers to record its business activities, including sales. The corporation ceased doing business on March 14, 2006.

On March 3, 2004, the Division of Taxation ("Division") sent to the corporation a letter indicating that a sales and use tax audit of the business's books and records for the period June 1, 2001 through February 28, 2004 was scheduled for April 16, 2004. The letter requested that all books and records pertaining to the corporation's sales and use tax liability for the period under audit be made available on the appointment date. These records were to include journals, ledgers, sales invoices, purchase invoices, cash register tapes, guest checks, exemption certificates, Federal income tax returns, New York State income tax returns, business checking account bank statements, bank deposit slips, and sales and use tax returns.

Following petitioner's cancellation of the initial meeting with the auditors, his failure to appear at the subsequent meeting and his failure to produce any books and records, the auditors contacted petitioner's landlord, Division Enterprises, and requested a copy of the lease for the period June 1, 2001 through February 28, 2004. Division Enterprises (a/k/a Westview Associates and West 72nd Street Associates) sent a letter to the auditors, dated March 6, 2000, indicating the annual rent to be as follows:

PERIOD	ANNUAL RENT	MONTHLY RENT
3/1/00 - 2/28/02	\$47,000.00	\$3,916.66
3/1/02 - 2/28/04	\$50,000.00	\$4,166.66
3/1/04 - 2/28/05	\$53,000.00	\$4,416.66

The auditor determined a rent factor by using the Almanac of Business and Industrial Financial Ratios, 1997 Edition. The Almanac indicated that for a pasta restaurant/pizza take-out establishment, rent should be 11.4% of operating costs or operating income. By applying the

amount of rent paid by petitioner per quarter and dividing the amount by the 11.4% rent factor, the auditor computed Natural Health's adjusted taxable sales. Reported taxable sales were deducted from adjusted taxable sales to arrive at additional taxable sales. Additional taxable sales for the audit period were determined to be \$914,873.00, resulting in additional tax due of \$76,492.28.

A Statement of Proposed Audit Changes was sent to the corporation at its address on June 2, 2004. The statement was returned to the Division on June 16, 2004 marked "delivery attempted, addressee unknown." Failing to obtain a forwarding address for the business, the auditor sent the statement to petitioner's home address, 35-29 Crescent Street, Long Island City, New York 11106. The auditor had obtained this address from petitioner in an earlier telephone conversation.

On July 26, 2004, the Division issued to Natural Health Food a Notice of Determination of sales and use taxes due assessing tax in the amount of \$76,492.28 for the period June 1, 2001 through February 28, 2004, plus penalty and interest. Penalties pursuant to Tax Law § 1145(a)(1)(i) and (vi) were assessed based upon the large amount of underreporting, the failure to provide books and records and the underreporting of tax due in excess of 25% of the amount of sales and use tax that should have been reported. On the same date, the Division issued to petitioner a Notice of Determination of sales and use tax assessing tax due of \$76,492.28 for the period June 1, 2001 through February 28, 2004. Interest and penalties pursuant to Tax Law § 1145(a)(1)(i) and (vi) were also assessed. Petitioner was assessed as an officer or responsible person of Nature Health Food pursuant to Tax Law §§ 1131(1) and 1133.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge discussed the standard for reviewing a sales tax audit where external indices are employed. He noted that a vendor is required to maintain complete, adequate and accurate books and records and, upon request, to make the same available for audit by the Division. The Administrative Law Judge stated that where insufficient records are kept and it is not possible to conduct a complete audit, the tax may be estimated on the basis of external indices where the Division need only adopt an audit method reasonably calculated to determine the amount of tax due, but exactness is not required (*see, Matter of Meyer v. State Tax Commn.*, 61 AD2d 223 [1978], *lv denied* 44 NY2d 645 [1978]). The burden is then on the taxpayer to demonstrate, by clear and convincing evidence, that the audit method employed or the tax assessed was unreasonable (*see, Matter of Meskouris Bros. v. Chu*, 139 AD2d 813 [1988]).

The Administrative Law Judge found that the record in this case established that the Division made clear, unequivocal written requests for the books and records of the corporation's sales and that petitioner failed to produce any such books and records for the Division's review. As a result, the Administrative Law Judge found that the auditor reasonably concluded that the business did not maintain books and records that were sufficient to verify its gross and taxable sales for the audit period. Having established the insufficiency of the books and records, the Division resorted to using the method of a projection based on the amount of rent petitioner paid for the business location. Such method is specifically provided for under the second sentence of Tax Law §1138(a)(1), and its application by the Division has been upheld as valid in numerous instances (*see, Matter of A&J Gifts Shop v. Chu*, 145AD2d 877 [1988], *lv denied* 74NY2d 603 [1989]). The Administrative Law Judge noted that petitioner's claim in this proceeding is that the auditors refused to examine the books and records he maintained. The Administrative Law

Judge found that this claim is not borne out by the testimony or documentary evidence in the record. Accordingly, the only issue for the Administrative Law Judge to determine was whether petitioner established that the amount of tax assessed as the result of the application of the Division's method of audit was erroneous.

The Administrative Law Judge noted that subsequent to the hearing, petitioner produced bank statements for the months of October 2003 through February 2004, purchase receipts for some of the audit period, photographs depicting the business premises, canceled checks for a portion of the audit period and a landlord tenant answer document from the Civil Court of the City of New York relating to a dispute between petitioner and his landlord for the month of August 2002. The Administrative Law Judge determined that the records petitioner provided were insufficient to conduct an audit of the business in order to verify the correct amount of its sales. Further, despite the use of a cash register to record business activity, including sales, cash register tapes were not provided. The purchase records did not contain internal controls to determine if they represented the business's complete purchases for the period provided. The Administrative Law Judge pointed out that there was no source documentation provided that could assist in the determination of the correct amount of the business operation's sales during the audit period.

Petitioner argued that his landlord reduced his monthly rent by approximately 10%, due to a disagreement over scaffolding that the landlord had erected over petitioner's business. In support of this allegation, petitioner produced two canceled checks showing payment to West 72nd Street Associates for the months of December 2003 and January 2004. The rental checks presented by petitioner for the months noted above, were for the same amounts as indicated in the letter provided by the landlord to the auditor. More importantly, the Administrative Law Judge noted

that additional checks were written by petitioner during the months of October and November 2003 to the landlord, to make up the difference between the above-noted checks and the rent due as indicated in the landlord's letter. The Administrative Law Judge determined that petitioner failed to establish any reduction in the amount of his rent during the audit period to warrant a reduction in the sales and use tax assessed.

Petitioner objected to the Division's audit result because it was imprecise. The Administrative Law Judge pointed out that any imprecision in the results of an audit arising by reason of a taxpayer's own failure to keep and maintain records of all of its sales as required by Tax Law §1135(a)(1) must be borne by the taxpayer (*see, Matter of Markowitz v. State Tax Commn., supra; see also, Matter of Meyer, supra*). In the instant matter, petitioner specifically complained that the auditor's review of his records might have yielded a more accurate result. The Administrative Law Judge determined that the complete absence of any original sales records left the Division clearly justified in the method of audit chosen. Moreover, petitioner's suggested alternative that the auditor should have reviewed his records overlooks the fact that petitioner provided no records to establish the basis of the sales reported, and no source documentation which would have provided the Division with the means to verify the sales reported.

The Administrative Law Judge determined that neither the documentation nor the testimony presented by petitioner rose to a level of clear and convincing evidence sufficient to show that the assessment was erroneous or that the audit methodology was unreasonable (*see, Matter of Scarpulla v. State Tax Commn.*, 120 AD2d 842 [1986]; *Matter of Surface Line Operators Fraternal Org. v. Tully* 85 AD2d 858 [1981]). The Administrative Law Judge determined that there is no reason to believe that the documentation is sufficiently accurate to

establish that the audit based upon the rent factor reached an erroneous result. The Administrative Law Judge noted that had petitioner been able to demonstrate through source documentation that the reported sales were more accurate than the Division's estimate generated by the rent factor, petitioner's contentions might have had more credibility. But the inadequate and otherwise nonexistent records gave the Division the authority to use a method, which, although less than precise, was reasonably calculated to reflect the taxes due, and nothing that was produced or said clearly or convincingly challenged the audit methodology or the amount of tax determined to be due.

The Administrative Law Judge found that petitioner failed to provide evidence that would support reduction or abatement of the penalties imposed and, therefore, penalties were sustained. The Administrative Law Judge noted that in establishing reasonable cause for penalty abatement, the taxpayer faces an onerous task (*see, Matter of Philip Morris, Inc.*, Tax Appeals Tribunal, April 29, 1993). Here, the Administrative Law Judge observed that petitioner neither maintained nor produced records as required, and those that were provided were without any source documentation due to the lack of cash register receipts. Further, there was a substantial discrepancy between reported sales and audited sales as evidenced by the tax paid with the returns during the audit period and the tax found due as a result of the audit. Accordingly, the Administrative Law Judge found that petitioner has provided no basis upon which penalties, properly imposed, should be reduced or abated and therefore the penalties must be sustained.

ARGUMENTS ON EXCEPTION

Petitioner, on exception, argues as he did below that the landlord reduced his monthly rent by approximately 10%, which should warrant a reduction in the sales and use tax assessed. Petitioner also argues that the Division's audit method and result was imprecise. Petitioner

maintains that all sales tax liabilities due to New York State have been fully paid. The Division asserts that petitioner makes the same arguments on exception as were addressed and dismissed by the Administrative Law Judge as being without factual support and legal basis. The Division requests that the exception be denied and the notice be sustained in full.

OPINION

We affirm the determination of the Administrative Law Judge for the reasons stated therein. The Administrative Law Judge fully and properly addressed the issues raised by petitioner. Petitioner has produced no evidence below, nor arguments on exception, that would justify our modifying the determination of the Administrative Law Judge in any respect.

Accordingly, it is ORDERED, ADJUDGED, and DECREED that:

1. The exception of Michael Constantini is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Michael Constantini is denied; and
4. The notice of determination dated July 26, 2004 is sustained.

DATED: Troy, New York
January 10, 2008

/s/ Charles H. Nesbitt
Charles H. Nesbitt
President

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

/s/ Robert J. McDermott
Robert J. McDermott
Commissioner