

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition :  
of :  
WILLIAM D. BARTON : DETERMINATION  
OFFICER OF DATEL SYSTEMS CORPORATION :  
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, 1980 :  
through February 28, 1983. :

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Petitioner, William D. Barton, Officer of Datel Systems Corporation, 201 East 83rd Street, New York, New York 10028, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1980 through February 28, 1983 (File No. 801445).

A hearing was commenced before Brian L. Friedman, Hearing Officer, at the offices of the former State Tax Commission, Two World Trade Center, New York, New York, on June 19, 1986 at 1:15 P.M. and was continued to conclusion before Brian L. Friedman, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on August 29, 1988 at 1:15 P.M., with all briefs to be submitted by February 1, 1989. Petitioner appeared at the June 19, 1986 hearing by Schwartz, Klink & Schreiber, P.C. (Cindy V. Schlaefer, Esq., of counsel) and at the August 29, 1988 hearing by Milgrim, Thomajan & Lee, P.C. (James A. Guadiana, Esq., of counsel). The Division of Taxation appeared at the June 19, 1986 hearing by John P. Dugan, Esq. (Joseph W. Pinto, Jr., Esq., of counsel) and at the August 29, 1988 hearing by William F. Collins, Esq. (Michael J. Glannon, Esq., of counsel).

ISSUES

I. Whether William D. Barton was a person required to collect sales and use taxes on behalf of Datel Systems Corporation within the meaning and intent of Tax Law §§ 1131(1) and 1133(a) for the period at issue herein.

II. If so, whether the Division of Taxation properly determined the sales and use taxes due from Datel Systems Corporation for the period at issue herein.

FINDINGS OF FACT

1. Pursuant to a field audit of Datel Systems Corporation ("Datel") which commenced in March 1983, the Division of Taxation, on June 8, 1984, issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due to William D. Barton ("petitioner"), as officer of Datel, in the amount of \$41,312.91, plus interest, for a total amount due of \$51,214.55 for the period September 1, 1980 through February 28, 1983. The notice of determination advised petitioner that he was personally liable as an officer of Datel under Tax Law §§ 1131(1) and 1133.

2. On November 19, 1983, Datel, by its president, executed a consent extending the period of limitation for the assessment of sales and use taxes whereby he agreed, on behalf of Datel, that such taxes due for the period September 1, 1980 through February 28, 1981 could be assessed at any time on or before June 20, 1984.<sup>1</sup>

3. Datel was engaged in retail sales of computer hardware and software to individuals, corporations and small businesses. During the audit period, the corporation maintained two stores and its administrative offices at 1211 Avenue of the Americas in New York City.

4. During the course of the audit, the auditor met primarily with and was supplied with the corporation's books and records by the corporation's controller, Raj Patel. At the time of the commencement of the audit, records for the entire audit period were requested and, with the exception of some documentation to support Datel's claimed nontaxable sales, all records requested were provided to the auditor. The audit actually consisted of an examination in three areas, i.e., fixed assets (fixtures, equipment and leasehold improvements), recurring expense purchases and sales. With respect to fixed assets, a detailed audit of Datel's books and records was performed resulting in the auditor's determination that fixed asset purchases of \$81,639.28, upon which sales tax had not been paid, were subject to tax. By applying the statutory rate in effect for the particular periods at issue, additional tax due in the amount of \$6,734.13 was assessed thereon.

While books and records relative to expense purchases and sales were available for the entire audit period, the auditor discussed with Mr. Patel the possibility of performing a test-period audit of these expense purchases and sales. At the recommendation of Mr. Patel, petitioner, as president of Datel, executed an Audit Method Election form on May 6, 1983 whereby he elected the utilization of a representative test period audit method to determine the corporation's sales or use tax liability despite the fact that Datel's records available for audit were adequate and sufficient to perform a detailed audit of expense purchases and sales.

5. Pursuant to the instructions of his supervisor, the auditor selected the month of November 1982 as the test period for the audit of Datel's expense purchases and sales. The primary reason for selection of this month was that the auditor and his supervisor felt that there existed a substantial number of invoices for examination. The auditor stated that neither Mr. Patel nor anyone else on behalf of the corporation objected to the use of the test period selected. It was determined that some office supplies had been purchased without the payment of sales tax during the test period. An error rate of 42.27 percent was calculated which, when applied to expense purchases of \$18,850.40, resulted in a determination by the auditor that Datel had made purchases in the amount of \$7,968.00 upon which tax was unpaid. Additional tax due calculated thereon was \$650.16.

With respect to the audit of the corporation's sales, approximately 300 invoices for November 1982 were examined. Of these 300 invoices, 36 invoices related to claimed nontaxable sales. Initially, 22 of the 36 invoices were disallowed by the auditor as unsubstantiated. An error rate of 30.924 percent was computed (\$37,897.07 disallowed, divided

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<sup>1</sup>It is not clear, from the signature on the consent, who signed this document on behalf of Datel. Petitioner had, however, left the corporation on November 8, 1983 and, at that time, vacated his position as president.

by \$122,547.28 in total nontaxable sales for November 1982, equals .30924) and was applied to total nontaxable sales for the audit period (\$3,210,555.00), resulting in disallowed nontaxable sales of \$992,832.00 for the period. Tax due thereon, at the appropriate statutory rate, was determined to be \$81,252.10. When added to tax due on fixed asset purchases (\$6,734.13) and expense purchases (\$650.16), total additional tax due was \$88,636.39. On September 16, 1983, a Statement of Proposed Audit Adjustment, asserting additional tax due of \$88,636.39 was issued to Datel. By a letter dated October 11, 1983, C. E. Morgan, vice-president of operations and service, disagreed with the findings set forth on the Statement of Proposed Audit Adjustment.

6. On November 9, 1983, an informal conference was held at the auditor's office. Pursuant to this conference and the auditor's acceptance of documentation for certain (7 sales invoices) of the previously disallowed nontaxable sales, a revised error rate of 12.913 percent was computed. By applying this revised error rate to total nontaxable sales for the audit period (\$3,210,555.00), total disallowed nontaxable sales were determined to be \$414,579.00, with tax due thereon in the amount of \$33,928.62. When added to tax due on fixed asset purchases (\$6,734.13) and expense purchases (\$650.16), total additional tax due, pursuant to the revised computations, was found to be \$41,312.91 (the amount of the assessment issued to petitioner on June 8, 1984).

7. The primary basis for the issuance of the assessment to petitioner was an examination of Datel's Federal income tax returns for 1980 through 1982 on which petitioner was listed as an officer who devoted 100 percent of his time to the business, owned 40 percent of the common stock and received compensation of \$40,694.00, \$44,789.00 and \$61,250.00, respectively, for each of these years. In addition, petitioner's signature appeared on nearly all of the corporation's sales tax returns filed during the audit period and on corporate checks issued for payment of Datel's tax liabilities.

8. Petitioner was the founder of Datel and was its chief financial officer during his employment with the corporation from November 8, 1978 through November 8, 1983. During this period, he served as corporate president and also as a director. His primary duties were to promote the company, obtain corporate financing, procure sales and manage both the operation and the corporate personnel. Petitioner had the authority to and did hire and fire personnel at all levels, and he had authority to sign corporate tax returns. With the exception of temporary authority granted by petitioner to Marjorie Yellon, assistant treasurer, in his absence, petitioner had sole authority to sign corporate checks.

9. During the early stages of the audit (April and May 1983), approximately 50 percent of petitioner's workday was spent preparing Datel's shares for public offering, the purpose of which was to obtain adequate financing for the corporation which, at that time, was undercapitalized. Datel had been the first computer retailer to carry IBM products but, due to its financial condition, was unable to pay its vendors and, subsequently, lost IBM as a supplier. This was the primary cause for petitioner's leaving the corporation in November 1983. After November 1983, petitioner was no longer an officer or director of Datel, but continued as a shareholder. Prior to the public offering, petitioner owned 40 percent of the corporate stock; afterward, he owned 22 percent.

10. During petitioner's tenure with Datel, its sales tax returns were prepared and/or reviewed by its accounting firm, Arthur Young & Co., in concert with the corporation's controller, Raj Patel. The corporation's sales department was responsible for collecting sales tax on taxable sales, obtaining exemption documents for nontaxable sales and turning over the tax or exemption documents to the accounting department (Mr. Patel and his supervisor, Peter Sattin,

Vice President-Finance). Petitioner received the sales tax returns for the purpose of affixing his signature thereto. Due to the fact that Datel had undergone a previous sales tax audit for the period September 1, 1978 through August 31, 1980, petitioner was aware of and impressed upon his employees the corporation's responsibility for collecting tax and securing exemption documents. Datel maintained a separate bank account at the Barclay Bank for the deposit of State and Federal taxes. Approximately eight percent of daily receipts were deposited into this account.

### SUMMARY OF PETITIONER'S POSITION

11. Petitioner contends that the Division of Taxation's utilization of a test-period audit was arbitrary and capricious due to the fact that complete books and records were available for the entire audit period.

12. Petitioner further contends that, even if a test-period audit was permissible, the test period (November 1982) utilized by the auditor was not representative of the corporation's sales since its products were sold in greater volume during this period to individuals who purchased computers for Christmas gifts and to businesses which chose to make year-end purchases to expend budget dollars and to utilize investment credits. Petitioner alleges that he voiced his objection to the use of this one-month test period to Mr. Patel and that he and other corporate officers unsuccessfully attempted to convince the auditor to utilize a longer (at least three months) period for the performance of his test-period audit.

13. While petitioner concedes that he was an "active" corporate officer, he contends that he should not be held personally liable for payment of Datel's sales tax liability because the responsibility for collection of tax and exemption documents had been delegated to the corporation's controller (Raj Patel), vice president - finance (Peter Sattin) and vice president - operations (Charles Morgan). In support of his position, petitioner cites certain Federal court decisions which address the issue of "willfulness". Moreover, petitioner alleges that despite his strict instructions to corporate officers and sales department employees to collect tax or obtain substantiation of nontaxable sales, some employees nevertheless, failed to comply with petitioner's instructions. (Sales by one particular salesman, no longer employed by Datel at the time of the audit, accounted for the majority of claimed nontaxable sales for which no documentation had been obtained.)

### CONCLUSIONS OF LAW

A. The first issue to be addressed herein is whether the Division of Taxation properly determined that petitioner was a person required to collect sales and use taxes on behalf of Datel for the period at issue.

Tax Law § 1133(a) provides, in part, that every person required to collect the taxes imposed under Article 28 of the Tax Law is also personally liable for the tax imposed, collected, or required to be collected under such law. Tax Law § 1131(1) defines "(p)ersons required to collect tax", as used in Tax Law § 1133(a), to include any officer or employee of a corporation or a dissolved corporation who, as such officer or employee, is under a duty to act for the corporation in complying with any requirement of Article 28 of the Tax Law.

The determination of whether an individual is a person or officer under a duty to act for the

corporation is based upon the facts presented (Vogel v. New York State Department of Taxation and Finance, 98 Misc 2d 222). The relevant factors include, but are not limited to: the individual's daily involvement in the corporation; the individual's participation and involvement in the financial affairs of the corporation; whether the individual prepared and signed the sales and use tax returns; the individual's authority to draft checks on the firm's bank account; and, in the case of a closely-held corporation, the individual's knowledge of the affairs of the firm and benefits from the firm's profits (Matter of Robert Gattie, State Tax Commission, September 5, 1980). Applying these factors to the present matter results in a determination that petitioner was a person required to collect sales and use taxes on behalf of Datel. Petitioner was the president, the chief financial officer and a director of Datel for the entire audit period. He had the authority to and did hire and fire personnel at all levels and sign corporate tax returns. With some limited exceptions, petitioner had the sole authority to sign corporate checks. He was a full-time employee of Datel and derived substantial income (both from salary and status as a shareholder) therefrom. Petitioner, admittedly, was fully aware of the corporation's responsibility for collecting sales and use taxes. Such awareness had been increased due to a prior sales tax audit of Datel for a period immediately preceding the period at issue herein.

Petitioner contends that he had delegated various responsibilities for collection of Datel's sales and use tax liabilities to other corporate officers and personnel and, as such, should not be held personally liable for sales and use tax assessments against Datel and that, even if held to be a person required to collect the tax, his failure to collect and remit such taxes was not willful. "[C]orporate officials responsible as fiduciaries for tax revenues cannot absolve themselves merely by disregarding their duty and leaving it to someone else to discharge" (see, Ragonesi v. State Tax Commn., 88 AD2d 707, 708; Capoccia v. State Tax Commn., 105 AD2d 528, 529). Moreover, "willfulness" is not a factor to be considered in determining whether a corporate officer is a person required to collect the taxes imposed by Article 28 of the Tax Law.

B. Tax Law § 1138(a) (former[1]) provided, in pertinent part, that:

"If a return required by this article is not filed, or if a return when filed is incorrect or insufficient, the amount of tax due shall be determined by the tax commission from such information as may be available. If necessary, the tax may be estimated on the basis of external indices...."

Such external indices may not be utilized unless it is "virtually impossible to verify taxable sales receipts and conduct a complete audit" with available records (Matter of Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 46; see also, Matter of Christ Cella, Inc. v. State Tax Commn., 102 AD2d 352). The Division of Taxation has conceded that Datel maintained adequate and sufficient records for the audit period and, therefore, did not utilize external indices due to the impossibility of conducting a complete audit. Instead, such indices (in the present matter, a test-period audit) were employed pursuant to a written agreement between the auditor and an authorized representative of Datel, i.e., petitioner as president. Although petitioner was not an active participant in the audit (Datel's controller, Raj Patel, was assigned to work with the auditor in this matter), he did, in fact, execute the Audit Method Election form on behalf of Datel, presumably after conferring with Mr. Patel. Petitioner has, therefore, agreed to the employment of a test-period audit and may not now claim that the Division of Taxation must conduct a complete audit of the books and records of Datel.

C. The Audit Method Election form signed by petitioner did, however, contain the following explanation:

"It is understood that this agreement pertains to the audit method to be used to conduct the audit; that is, a test period audit as described on the reverse side of this form. Agreement with the test period audit method does not in any way constitute a consent to the audit findings or preclude the protest of the audit results on grounds such as the particular test period selected, the inclusion of certain transactions within the test, the taxability of certain transactions or the method of projecting the results of the test period findings."

It is clear, therefore, that while petitioner may not challenge the audit method utilized, he may contest the audit results. As indicated in Paragraph "12", supra, petitioner is challenging the auditor's use of the month of November 1982 as too limited to be a representative sample and, in addition, as a month in which sales were near or at their peak for the year. The burden rests, however, upon petitioner to demonstrate by clear and convincing evidence that the particular test period selected (November 1982) resulted in an erroneous assessment (Matter of Surface Line Operators Fraternal Organization v. Tully, 85 AD2d 858).

With respect to petitioner's contention that a one-month test period was too limited to be a representative sample, petitioner has presented no evidence to support this contention. While it is true that, as of the date of the issuance of the assessment, petitioner was no longer an officer or director of Datel and, as a result thereof, perhaps no longer had access to Datel's books and records, he has not shown any diligent attempts (by subpoena or otherwise) to obtain the books and records and/or to have them produced at the hearing held herein. The Division of Taxation conceded, by means of the Audit Method Election form, that, on May 6, 1988, adequate and sufficient books and records existed for the audit period. Mere allegations that petitioner and other corporate officers attempted to dissuade the auditor from employing a one-month test period are not sufficient to prove that the audit results were erroneous due to the limited test period selected by the auditor.

Petitioner's other contention, i.e., that November 1982 was not representative of Datel's sales because its products were sold in greater volume than during most all other months (except December) also fails, absent records to substantiate such contention, to constitute clear and convincing evidence of an erroneous assessment. It should also be noted that petitioner's objections to the audit do not concern gross sales but rather the disallowance of nontaxable sales. The resulting assessment thereon represents approximately 82 percent of the entire assessment. The evidence is uncontroverted that November 1982 was selected because of the existence of what the auditor categorized as a substantial number (approximately 300) of invoices for this month. Out of the total number of invoices examined, only 36 related to claimed nontaxable sales. Initially 22, and after an informal conference, 15 of these invoices were disallowed as nontaxable by the auditor. In order to sustain his burden of proving that the assessment was erroneous on the basis of the selection of an inordinately high-volume month, petitioner must also show that either claimed nontaxable sales were unusually high for this month or, in the alternative, that an unusually large number of nontaxable sales took place during the month, the disallowance of which could have a large effect on the accuracy of the projection (see, Yonkers Plumbing and Heating Supply Corp. v. Tully, 62 AD2d 18). Absent records, petitioner was unable to substantiate this second contention.

D. The petition of William D. Barton, officer of Datel Systems Corporation, is denied and the Notice of Determination and Demand for Payment of Sales and Use Taxes Due issued on June 8, 1984 is sustained in its entirety.

DATED: Albany, New York  
February 24, 1989

/s/ Brian L. Friedman  
ADMINISTRATIVE LAW JUDGE