STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition

of

ABERBACH ENTERPRISES, LTD.
D/B/A ABERBACH FINE ART

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, 1983 through May 31, 1986.

In the Matter of the Petition

of

JULIAN ABERBACH
OFFICER OF ABERBACH
ENTERPRISES, LTD.

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, 1983 through May 31, 1986.

In the Matter of the Petition

of

JOACHIM (JEAN) ABERBACH
OFFICER OF ABERBACH
ENTERPRISES, LTD.

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, 1983 through May 31, 1986.

DETERMINATION

Petitioners Aberbach Enterprises, Ltd., 980 Madison Avenue, New York, New York 10021, Julian Aberbach, as officer of Aberbach Enterprises, Ltd., 7 Lott Avenue, West Hampton Beach, New York 11978, and Joachim (Jean) Aberbach, as officer of Aberbach Enterprises, Ltd., 33 Bacon Road, Old Westbury, New York 11568, filed separate petitions for revision ofdeterminations or for refunds of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1983 through May 31, 1986 (File Nos. 807509, 807510 and 807511).

A consolidated hearing was held before Jean Corigliano, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on May 8, 1990 at 9:15 A.M., and the record was closed to submission of briefs on January 3, 1991. Petitioners appeared by Robert Bandman, C.P.A. The Division of Taxation appeared by William F. Collins, Esq. (Robert J. Jarvis, Esq., of counsel).

ISSUES

I. Whether petitioners have shown that the audit results were inaccurate.

II. Whether petitioners have established reasonable cause for cancellation of penalties.

FINDINGS OF FACT

Petitioner Aberbach Enterprises, Ltd. operates an art gallery in New York City doing business under the name Aberbach Fine Art. A sales tax field audit of Aberbach's books and records for the period September 1, 1983 through May 31, 1986 began in May 1986. At that time, a field audit appointment letter was sent to Aberbach, requesting that all records pertaining to Aberbach's sales tax liabilities for the audit period be made available to the Division of Taxation ("Division") for its review.

Initially, the auditor communicated with Aberbach's bookkeeper, a woman named Patricia Gallagher. She informed the auditor that all records necessary for audit were available. On July 2, 1986, at the auditor's request, Ms. Gallagher provided the auditor with records for the sales tax quarterly periods ended May 31, 1984 and November 30, 1985. Soon thereafter, Ms. Gallagher died. The auditor's log does not reveal whether he was informed of Ms. Gallagher's death; however, it does show that in August 1986, the auditor spoke with several different representatives of Aberbach who asked for postponements of the audit and stated that Aberbach was having some difficulty in assembling the records required for audit. The log also shows that by August 19, 1986, a new bookkeeper, Paula Glass, had been appointed by Aberbach.

The records eventually made available included: Federal and State income tax returns, a sales journal, a general ledger, a check disbursements journal, a great many sales invoices, resale certificates and shipping documents. It is difficult to determine exactly which records were and were not available because of inconsistencies in the proof offered at hearing. For instance, the auditor's checklist of available books and records indicates that a general ledger was not available, but the determination of tax due relied, in part, on a comparison of figures found in the general ledger and the sales journal. Although the auditor indicated that Aberbach's books and records were in only "fair" condition, the evidence does not establish in what way the records were deficient, other than the failure to maintain complete shipping documents.

The audit found tax due in three areas: $444.97 was determined to be due on Aberbach's recurring expense purchases; $1,103.61 was determined to be due on Aberbach's purchases of fixtures and equipment; and $89,958.74 was determined to be due on additional taxable sales by Aberbach. Petitioners do not challenge the determinations of tax due in the first two areas; therefore, the remainder of this determination treats only the Division's audit of Aberbach's sales.

The Division determined Aberbach's tax liability based on a detailed audit of petitioners' books and records. Aberbach reported gross sales for the audit period of $5,125,336.00 and taxable sales of $398,463.00 which yields nontaxable sales of $4,726,873.00. The audit began then with a review of Aberbach's records to determine whether there was documentation to verify the claimed nontaxable sales. The auditor transcribed all sales posted to Aberbach's sales journal which did not show sales tax collected, thus calculating nontaxable sales per Aberbach's sales journal of $4,878,938.62. Information taken from the journal included the name and address of the customer, where shown, and the amount of the sale. The auditor then asked Aberbach to provide a sales invoice for each sale shown in the journal and proof that the sale was not subject to sales tax, such as a resale certificate or shipping documents showing delivery outside of New York. There is no evidence that Aberbach was unable to provide sales invoices for any of these sales. Based on a review of the sales invoices and related documentation, the auditor concluded that Aberbach was unable to substantiate the nontaxable status of sales in the amount of $2,308,592.97. A great majority of these appear to be sales to out-of-state customers for which Aberbach was unable to provide shipping documents or other evidence that the artwork was delivered out of state.

Aberbach's general ledger contained a monthly summary of sales. The auditor compared these monthly summaries with sales posted to the sales journal and found a discrepancy of $498,733.97 (total sales in this summary section of the general ledger amounted to $5,377,672.59). The discrepancy between sales per the general ledger and sales per the sales journal was treated as unreported sales subject to sales tax.

The Division then added unsubstantiated nontaxable sales to unreported sales to determine additional taxable sales of $2,807,326.94, with a tax due on that amount of $231,604.47. A statement of proposed audit adjustment in that amount was issued to Aberbach.

Following the issuance of the statement of audit adjustment, a conference was held between representatives of Aberbach and the Division. In preparing for the conference, the auditor realized that he made an error in calculating unreported sales. The auditor had transcribed from the sales journal only those sales upon which no sales tax was collected, and he had not transcribed those sales upon which Aberbach did charge and collect sales tax. In calculating unreported sales, the auditor had subtracted claimed nontaxable sales per the sales journal from gross sales (i.e., taxable and nontaxable sales) per the general ledger. Therefore, the discrepancy between the two was explained, at least in part, by the taxable sales posted to the sales journal. Since the auditor had not made a record of these, he could not perform an accurate reconciliation of the sales journal and general ledger. To overcome this problem, he added Aberbach's reported taxable sales (taken from Aberbach's filed sales tax returns) to the nontaxable sales shown in the sales journal to calculate gross sales per the sales journal ($398,463.00 + $4,878,938.62 = $5,277,401.62). This amount was subtracted from sales per the general ledger ($5,377,672.59) to calculate additional audited sales of $100,270.90. The

Division requested sales invoices documenting these sales. References in the audit report to missing sales invoices refer to these audited sales, determined on the basis of the discrepancy between the general ledger and the sales journal.

At the conference, Aberbach presented documentation which substantiated the nontaxable status of sales amounting to $1,318,455.00. To calculate additional taxable sales, the Division subtracted the sales shown to be nontaxable at this conference ($1,318,455.00) from additional taxable sales as originally calculated ($2,807,326.94). The result ($1,488,871.94) was further reduced by reported taxable sales ($398,463.00) to calculate additional taxable sales of $1,090,408.94, with a tax due on that amount of $89,958.74.

The Division issued two notices of determination and demands for payment of sales and use taxes due, dated April 27, 1988, to Aberbach. The first notice of determination assessed tax due for the period September 1, 1983 through May 31, 1986 of $91,517.04 plus penalty and interest. The second notice assessed an additional penalty for the period June 1, 1985 through May 31, 1986 in the amount of $2,851.45. Notices of determination assessing identical amounts of tax, penalty and interest were issued to Julian Aberbach and Jean Aberbach, as officers of Aberbach Fine Art. These notices of determination were timely issued as Aberbach had previously signed consents extending the period of limitation for the assessment of sales and use taxes.

Conciliation orders, dated August 11, 1989, were issued to petitioners, reducing the tax assessment to $90,716.30 and sustaining all penalties.

At hearing, petitioners introduced documentation into evidence which substantiated the nontaxable status of sales in the amount of $422,874.67.

(a) The Division treated as taxable two sales to Jan Krugier Galleries in the amounts of $55,000.00 (invoice no. 6994) and $110,000.00 (invoice no. 7298), respectively, on the ground that the resale certificate submitted bore the certificate of authority number of Chusa Art Development. Petitioners submitted a letter from Jan Krugier Galleries, establishing that Jan Krugier was the name under which Chusa did business.

(b) Sales shown on three different invoices (numbers 7044, 7063 and 7064), totalling $57,000.00, were proven to be not subject to sales tax, because the actual sale of the artworks took place outside the United States. The works of art in question were part of a larger group of paintings and sculptures shipped to museums in Colombia for exhibition. Many of these paintings and sculptures were sold in Colombia by the Museo De Arte Moderno de Bogota in Colombia, acting on behalf of Aberbach. Documents introduced by petitioners make it possible to trace the works of art shown on the invoices in question to an inventory of items shipped to Colombia in conjunction with this exhibition and, from there, to a list of items sold by the museum in Colombia and delivered to customers in Colombia.

(c) Invoice number 7245 shows a sale of a sculpture to Global Fine Arts, Ltd., for a price of $9,000.00. The invoice is dated October 18, 1984. Petitioners introduced a blanket resale certificate, dated February 4, 1985, from Global Fine Arts to Aberbach.

(d) Invoice number 7302 shows a sale in the amount of $5,000.00 to a customer in California. The customer was also charged a shipping fee of $12.50. Petitioners submitted two United Parcel Service receipts to substantiate that delivery of this item took place in California.

(e) Invoice number 7423, in the amount of $174,874.67, relates to a transaction between Aberbach and Thomas Gibson Fine Art, Ltd. of London. Aberbach purchased a sculpture by Alberto Giacometti in Paris for 680,000 Swiss Francs, or approximately $338,680.00 in March 1986. A half-interest in the sculpture was sold to Thomas Gibson for $174,874.67 (as documented by invoice number 7423). The sculpture was sold in December 1986 for $550,000.00 by the Thomas Gibson gallery in London to a European client. Thomas Gibson paid Aberbach $273,199.00 in December 1986, representing Aberbach's share of the sale price of the sculpture minus expenses. The sculpture did not enter New York State during this time. These transactions were fully documented by letters, invoices, bank statements and Aberbach's books of original entry.

(f) The final disputed invoice, number 7433, involves the sale of two works: "Rita at 5:30 p.m." for $18,000.00 and "Rita at 3:30 p.m." for $12,000.00. Both works are listed on the original invoice. Notations added to the invoice show that the sale of "Rita at 3:30" was cancelled, and the $1,000.00 deposit was applied to the customer's purchase of "Rita at 5:30". Thus, the total invoice amount should be reduced by $12,000.00.

Petitioners introduced two invoices (numbers 6925 and 7455) to demonstrate that the Division's finding of additional taxable sales based on the difference between sales in the general ledger and sales in the sales journal was erroneous. Invoice number 6925, dated November 22, 1983, shows a sale of two paintings for $61,000.00, with a $10,000.00 deposit. It also shows that this sale was canceled and the deposit applied to the purchase price of a sculpture as shown on a second invoice, number 7455, dated May 30, 1986. In calculating taxable sales from the sales journal, the auditor first listed invoice number 6925 and the amount of $61,000.00. Later, apparently upon review of the second invoice, he listed invoice number 6925 as a canceled sale and subtracted $61,000.00 from his totals. Thus, the auditor's calculations of sales per the sales journal accurately reflected the actual transactions. In calculating sales per the general ledger, however, the auditor referred only to the monthly sales summary and did not review adjusting entries or otherwise attempt to reconcile the various ledgers and books of original entry. Consequently, his calculations per the general ledger would not have reflected the cancelation of the $61,000.00 sale.

Petitioners also presented a letter from Saint Peter's College in New Jersey which established that the college is a not-for-profit corporation exempt from taxes under section 501(c)(3) of the Internal Revenue Code and that St. Peter's purchased paintings from Aberbach for $20,100.00 (invoice no. 6997) for use in a charitable program for the benefit of the college.

The vast majority of those transactions upon which Aberbach did not charge sales tax involved sales to persons or businesses located outside of New York. These were found to be taxable because Aberbach was unable to produce documentation, such as common carrier receipts, to show that the items were actually delivered to customers outside of New York. While not conceding that the deliveries took place in New York, petitioners acknowledge that they have been unable to provide proof that the items were shipped out of state. They point out that Aberbach's bookkeeper died shortly after this audit began and assert that their inability to locate the required shipping documents is attributable to the confusion in Aberbach's office caused by her death.

CONCLUSIONS OF LAW

A. Where a vendor fails to file a return required under article 28 of the Tax Law, or files a return which is incorrect or insufficient, the Division of Taxation is authorized to determine the tax due from such information as is available to it and may estimate the tax due on the basis of external indices if necessary (Tax Law § 1138[a][1]). Here, Aberbach's records were adequate and sufficient for the purpose of conducting a complete and detailed audit, and the tax due was determined on the basis of those records. Accordingly, the burden was on Aberbach to establish by clear and convincing evidence that the audit results were erroneous (see, Matter of A & J Gifts Shop v. Chu, 145 AD2d 877, 536 NYS2d 209, lv denied 74 NY2d 603, 542 NYS2d 518).

B. Petitioners established that Aberbach accurately reported its gross sales, and that there was no basis for that part of the Division's calculations which determined additional audited sales on the basis of a discrepancy between Aberbach's sales journal and general ledger. Petitioner established that the monthly summaries in the general ledger did not correctly state the exact amount of Aberbach's sales because no adjustments were made for canceled sales. In addition, Aberbach established that adjusting entries were made in other ledgers and journals which the Division failed to review. Aberbach introduced two invoices (numbers 6925 and 7455) which in themselves account for $61,000.00 of the alleged discrepancy of $107,270.90. Moreover, there is no evidence in the record to support the Division's conclusion that the difference between the general ledger monthly summaries and the sales journal, a figure which essentially was estimated by the Division (see, Finding of Fact "6"), represents unreported sales. Accordingly, the Division's calculation of additional taxable sales in the amount of $1,090,408.94 is to be reduced by $107,270.90.

C. Aberbach presented evidence which established the nontaxable status of sales in the amount of $422,874.67 (see, Finding of Fact "9"); therefore, additional taxable sales will be further reduced by this amount. Aberbach failed to prove the nontaxable status of a sale in the amount of $20,100.00 made to St. Peter's College in New Jersey. Section 1132(c) of the Tax Law creates a statutory presumption that receipts from all sales of tangible personal property are subject to tax unless the contrary is established by the person required to collect tax or the customer. Former section 1132(c), in effect at the time of the sale to St. Peter's College, states:

> "[u]nless...the purchaser prior to taking delivery, furnishes to the vendor: any affidavit, statement or additional evidence, documentary or otherwise, which the tax commission may require demonstrating that the purchaser is an exempt organization described in section eleven hundred sixteen, the sale shall be deemed a taxable sale at retail." (Emphasis added.)

Evidence that St. Peter's College was exempt from Federal income tax was not obtained until well after it took delivery of the art works. In addition, St. Peter's College offered no proof of exemption from New York State sales tax under Tax Law § 1116. "An exemption granted to an organization under section 501(c) of the Internal Revenue Code does not automatically exempt the organization under section 1116(a) of the Tax Law" (20 NYCRR 529.1[j][1]).

D. Tax Law § 1145(a)(1)(i) authorizes the imposition of penalty for failure to file a return or to pay over any tax imposed under the authority of article 28 in a timely manner. Section 1145(a)(1)(vi) imposes an additional penalty where the taxpayer omits from the total amount of taxes required to be shown on a return an amount which is in excess of 25 percent of the amount required to be shown on the return. In both cases, the penalty may be abated if the delay or failure to pay was due to reasonable cause and not due to willful neglect (Tax Law § 1145[a][1][iii], [vi]). The taxpayer bears the burden of establishing reasonable cause as well as the absence of willful neglect (see, e.g., Matter of T.V. Data, Inc., Tax Appeals Tribunal, March 2, 1989).

Reasonable cause includes:

> "[a]ny...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" (20 NYCRR 536.5[c][5]).

In determining whether reasonable cause exists, good faith and the extent of the taxpayer's efforts to ascertain the proper tax liability are important considerations (20 NYCRR 536.5[d][2]). Petitioners maintained adequate books and records of sales. The tax deficiency found by the Division is attributable, almost in its entirety, to petitioners' inability to provide evidence of out-of-state deliveries of certain art works. Petitioners established that the death of Aberbach's bookkeeper in the midst of this audit was the reason for their inability to gather and assemble the needed documentation. Inasmuch as petitioners have established that Aberbach properly maintained records of its sales, with the exception of shipping documents, good faith has been shown, and all penalties are cancelled.

E. The petitions of Aberbach Enterprises, Ltd. d/b/a Aberbach Fine Art, Julian Aberbach and Joachim (Jean) Aberbach are granted to the extent indicated in Conclusions of Law "B", "C" and "D"; the notices of determination and demands for payment of sales and use taxes due issued on April 27, 1988, shall be modified accordingly; and, in all other respects, the petitions are denied.

DATED: Troy, New York

3/14/91

ADMINISTRATIVE LAW JUDGE