STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
TANGO BOUTIQUE, INC. AND ROSALIND COOK AND JUDITH LASHIN, AS OFFICERS	:	DETERMINATION DTA NO. 809674
for Revision of Determinations or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period March 1, 1985 through November 30, 1987.	:	

Petitioners, Tango Boutique, Inc. and Rosalind Cook and Judith Lashin, as officers, 1305 Old Northern Boulevard, Roslyn, New York 11576, filed a petition for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period March 1, 1985 through November 30, 1987.

A hearing was held before Thomas C. Sacca, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on July 28, 1992 at 9:15 A.M. Petitioners filed a brief on September 9, 1992 and a reply brief on November 5, 1992. The Division of Taxation filed its brief on October 14, 1992. Petitioners appeared by DeGraff, Foy, Holt-Harris & Mealey (James H. Tully, Jr., Esq., of counsel) and S. Buxbaum and Company, P.C. (Stewart Buxbaum, CPA). The Division of Taxation appeared by William F. Collins, Esq. (Vera Johnson, Esq., of counsel).

ISSUES

I. Whether the sales tax field audit conducted by the Division of Taxation utilized an audit method reasonably calculated to reflect the taxes due.

II. Whether petitioners have shown that their failure to comply with the Tax Law, if so determined, was due to reasonable cause and was not due to willful neglect.

FINDINGS OF FACT

On July 5, 1989, the Division of Taxation ("Division") issued a Notice of Determination

and Demand for Payment of Sales and Use Taxes Due spanning the period March 1, 1985 through November 30, 1987 to petitioner Tango Boutique, Inc. ("Tango") assessing sales and use tax due in the amount of $271,997.28, plus penalty (Tax Law § 1145[a][1][i]) and interest. On the same date, the Division issued a notice of determination for the period June 1, 1985 through November 30, 1987 to Tango assessing a penalty of $25,037.67 pursuant to Tax Law § 1145(a)(1)(vi). On the same date, the Division issued identical notices of determination and demands for payment of sales and use taxes due spanning the same periods and assessing the same amounts as above to petitioners Rosalind Cook and Judith Lashin, as officers. The notices indicated that they were personally liable as officers of Tango for taxes determined to be due from the corporation. The notices were based upon the results of a field audit of the business operations of Tango as described hereinafter.

On August 27, 1988, petitioner Tango, by Judith Lashin, executed a consent having the effect of extending the period of limitations for assessment of sales and use taxes for the period March 1, 1985 through November 30, 1985 to March 20, 1989. On January 30, 1989, petitioner Tango, by Judith Lashin, executed a consent having the effect of extending the period of limitations for assessment of sales and use taxes for the period March 1, 1985 through February 28, 1986 to June 20, 1989. Finally, on May 19, 1989, petitioner Tango, by Rosalind Cook, executed a consent having the effect of extending the period of limitations for assessment of sales and use taxes for the period March 1, 1985 through May 31, 1986 to September 20, 1989.

On January 11, 1988, the Division sent a letter to Tango advising that the corporation's sales tax returns were scheduled for field audit. The period under audit was stated in the letter to be from December 1, 1984 to the "present". The letter requested that all books and records pertaining to the sales tax liability for the period under audit be made available. The books and records to be provided included journals, ledgers, sales invoices, purchase invoices, cash register tapes, exemption certificates and all sales tax records. Accompanying the appointment letter was a document entitled "Check List of Needed Records" which indicated the audit period

to be December 1, 1984 to the "present". The documents requested included the following:

General Ledger for audit period
Cash Receipts Journal for audit period
Cash Disbursements Journal for audit period
Federal Income Tax Returns for audit period
Sales Tax Returns and worksheets for audit period
Sales invoices for audit period
Expense purchase invoices for June - August 1987
All fixed asset invoices for fixed assets acquired during the audit period
Guest checks and cash register tapes for the audit period
Proof of out-of-state shipments for audit period

Petitioners provided the auditor with a general ledger for the audit period, a cash receipts journal covering the period May 1987 through November 1987, a cash disbursements journal relating to the period July 1987 through November 1987, Federal income tax returns for years that had been filed during the audit period, sales tax returns and worksheets for the last two quarters of the audit period, sales invoices for the period September 1987 through November 1987 and some fixed asset invoices. Proof of nontaxable sales was not originally provided.

Tango is in the retail women's apparel business and is located in Roslyn, New York. During the period at issue, Rosalind Cook was the president of Tango and Judith Lashin was its vice-president. The business began operating on February 28, 1977. At the beginning of the audit period, the business was located in a converted barn of approximately 1,300 square feet. The business advertised itself as a "discounter" of women's name-brand clothing, attracting clients by underselling the larger department stores. Petitioners provided testimony at the hearing that Tango attracted out-of-state customers by advertising in national magazines which resulted in sales throughout the country. In addition, according to testimony, out-of-state sales were generated by Tango shipping merchandise to its New York customers with second homes in Florida. As many of petitioners' local customers spent time in Florida, petitioners opened a store there sometime in 1986. However, the store was unsuccessful and closed within a year. The testimony further provided that merchandise that was shipped to customers both within and without New York State was handled by United Parcel Service ("UPS").

On March 1, 1987, the business's merchandise and records suffered substantial fire,

smoke and water damage as a result of an electrical fire in the building. All of the business's records were destroyed. Following the fire, the business moved to a new, larger location in Roslyn, New York. Petitioners' sales and use tax returns show that the business was active during the quarters ended May 31, 1987 and August 31, 1987, the two quarters immediately following the fire.

Petitioners employed a bookkeeper during the audit period. The bookkeeper would come into the store one or two days a week to maintain the records of the business. On the days the bookkeeper came into the store and the days she did not, the records were maintained in the same way. The sales slips from each day were attached to the daily cash register tape. The day's daily sales as shown on the cash register tape were recorded in the cash receipts journal. Following the daily bank deposit, the deposit slip would also be attached to the cash register tape and stored on a monthly basis in an envelope. The envelopes were placed in boxes and the boxes were stored in the business's attic. All of the records up to the date of the electrical fire were in the attic when the fire occurred, and they suffered extensive water damage. It is noted that the sales slips used by the sales people were not consecutively numbered nor was the information recorded on the slips sufficient to determine what item or items were being sold.

The purchases from the business's books were totalled and adjusted for the Florida store purchases and the insurance loss. These adjusted purchases were marked up by 66.67%, a percentage derived from the Dun & Bradstreet Cost of Doing Business and an index entitled "Almanac of Business Ratios". This markup percentage was applied to adjusted purchases to determine audited gross sales. As no documentation of nontaxable sales was presented, audited gross sales were considered to be taxable sales from which reported taxable sales were subtracted to arrive at additional taxable sales. This amount was multiplied by the applicable tax rate to yield sales tax due of $263,835.24. Petitioners were also assessed tax in the amount of $8,162.04 on fixed asset purchases for a total amount of tax due of $271,997.28.

Following the completion of the audit, petitioners provided the auditor with copies of UPS shipping documents for the last quarter of the audit period. These UPS shipping

documents were obtained by petitioners from UPS and presented to the auditor sometime in October 1988. In an attempt to verify these records, two auditors reviewed summary documents of petitioners' shipments as maintained by UPS. The summary documents indicated the week of pickup, the number of pickups, and the number of packages included in each pickup. The auditor compared the number of packages claimed to have been shipped by petitioners with the number shown on the UPS records, and found that the UPS records verified only 250 of the 285 packages claimed by petitioners. In an effort to verify the out-of-state sales of the last quarter, the auditor mailed a questionnaire to 47 of the UPS customers asking the customers if they had purchased merchandise from Tango, the amount of the purchase and where it was delivered. The auditor received 16 responses indicating delivery of merchandise out of state, although 8 of the envelopes had New York State postmarks. Ten of the questionnaires were returned as undeliverable and no response was received from 21 of the questionnaires. No adjustment was originally made to claimed nontaxable sales for the last quarter because no information, such as the amount purchased, was received from the customers that could be related back to the original sales slips.

On June 7, 1991, the Bureau of Conciliation and Mediation Services ("BCMS") issued a Conciliation Order revising the amount of tax, penalty and interest due. The revision was based upon a 13% disallowance of claimed nontaxable sales in the last quarter of the audit as computed by the auditor and based upon the UPS documents. The recomputation for the last quarter reduced the notice of determination for the period March 1, 1985 through November 30, 1987 to tax due of $260,697.92, plus applicable penalty and interest, and reduced the notice of determination for the period June 1, 1985 through November 30, 1987 for penalty assessed pursuant to Tax Law § 1145(a)(1)(vi) to $24,483.48. The allowance percentage was not applied to the earlier quarters because petitioners did not present any documentation of nontaxable sales for such quarters.

For the 4 sales and use tax quarters prior to the audit period and the 12 quarters of the audit period, Tango late filed three quarters, late paid eight quarters and partially paid four

quarters. The reason offered by petitioners for the failure to timely pay was that they were doing extensive buying for their new stores in Florida and Roslyn and did not have the money to pay the sales tax liability. Eventually, however, all sales tax liabilities were paid.

CONCLUSIONS OF LAW

A. The Division has the authority to determine, "from such information as may be available," the amount of tax actually due from a taxpayer for a given period when any one of its sales tax returns is either not filed or states an incorrect or insufficient amount of tax due (Tax Law § 1138[a][1]). When the vendor maintains a comprehensive set of books and records, "such information as may be available" (Tax Law § 1138[a][1]) is restricted to his books and records, and not external indicia, because "[t]he honest and conscientious taxpayer who maintains comprehensive records as required has a right to expect that they will be used in any audit to determine his ultimate tax liability" (Chartair, Inc. v. State Tax Commn., 65 AD2d 411 NYS2d 41, 43).

To determine the adequacy of a taxpayer's records, the Division must first request (Matter of Christ Cella v. State Tax Commn., 102 AD2d 352, 477 NYS2d 858, 859) and thoroughly examine (Matter of King Crab Restaurant v. State Tax Commn., 134 AD2d 51, 522 NYS2d 978, 979-80) the taxpayer's books and records for the entire period of the proposed assessment (Matter of Adamides v. Chu, 134 AD2d 776, 521 NYS2d 826, 828, lv denied 71 NY2d 806, 530 NYS2d 109). The purpose of the examination is to determine, through verification drawn independently from within these records (Matter of Meyer v. State Tax Commn., 61 AD2d 223, 402 NYS2d 74, 76, lv denied 44 NY2d 645, 406 NYS2d 1025; Matter of Giordano v. State Tax Commn., 145 AD2d 726, 535 NYS2d 255, 256-57; Matter of Urban Liquors v. State Tax Commn., 90 AD2d 576, 456 NYS2d 138, 139; see also, Matter of Hennekens v. State Tax Commn., 114 AD2d 599, 494 NYS2d 208, 209), that they are, in fact, so insufficient that it is "virtually impossible [for the Division] to verify taxable sales receipts and conduct a complete audit" (Chartair, Inc. v. State Tax Commn., supra, 411 NYS2d at 43; Matter of Christ Cella v. State Tax Commn., supra), "from which the exact amount of tax due can be determined"

(Matter of Mohawk Airlines v. Tully, 75 AD2d 249, 429 NYS2d 759, 760).

Where the Division follows this procedure, thereby demonstrating that the records are incomplete or inaccurate, the Division may resort to external indices to estimate tax (Matter of Urban Liquors v. State Tax Commn., supra). The estimate methodology utilized must be reasonably calculated to reflect taxes due, but exactness is not required from such a method (Matter of W. T. Grant Co. v. Joseph, 2 NY2d 196, 159 NYS2d 150, 157, cert denied 355 US 869; Matter of Markowitz v. State Tax Commn., 54 AD2d 1023, 388 NYS2d 176, 177, affd 44 NY2d 684, 405 NYS2d 454).

B. It is clear and not in dispute that Tango did not have adequate books and records at the time they were requested by the Division, and therefore the Division had the right to use an estimate methodology. The issue to be decided is whether petitioners have established by clear and convincing evidence that the nontaxable adjustment should be made to the remaining portion of the audit (see, Matter of Ristorante Puglia, Ltd. v. Chu, 102 AD2d 348, 478 NYS2d 91; Matter of House of Audio of Lynbrook, Tax Appeals Tribunal, January 2, 1992).

C. There is a statutory presumption pursuant to Tax Law § 1132(c) that certain types of sales are taxable[1] (see, Matter of Sol Wahba v. New York State Tax Commn., 127 AD2d 943, 512 NYS2d 542 [retail sales of electronic equipment]; Matter of Sunny Vending Co. v. State Tax Commn., 101 AD2d 666, 475 NYS2d 896 [cafeteria sales]; Matter of LaCascade, Inc. v. State Tax Commn., 91 AD2d 784, 458 NYS2d 80 [sale of vacation packages in "lump sum" rates]; Matter of Goldner v. State Tax Commn., 70 AD2d 978, 418 NYS2d 477, lv denied 48 NY2d 608, 423 NYS2d 1025 [deli sales]; Matter of Reference Lib. Guild, Tax Appeals Tribunal, August 4, 1988 [out-of-state sales]). This presumption does not satisfy the Division's

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[1]Tax Law § 1132(c) provides, in pertinent part, that:

> "[i]t shall be presumed that all receipts for property or services of any type mentioned in subdivisions (a), (b), (c) and (d) of section eleven hundred five . . . are subject to tax until the contrary is established, and the burden of proving that any receipt . . . is not taxable hereunder shall be upon the person required to collect tax . . . ."

burden to devise a reasonable methodology for calculating taxable sales. The method used by the Division must be evaluated under all of the circumstances existing at the time of the audit. The determining factor is whether, during the audit, petitioners provided the Division with the records relating to nontaxable

sales for the audit quarter after the fire (see, Matter of Bernstein-On-Essex St., Tax Appeals Tribunal, December 3, 1992; Matter of Auriemma, Tax Appeals Tribunal, September 17, 1992; Matter of House of Audio of Lynbrook, supra).

The record indicates that the books and records for the nontaxable sales for the audit period were requested by the auditor and that petitioners eventually provided records substantiating nontaxable sales for the quarter ended November 30, 1987. However, the record also indicates that the business operated and filed sales tax returns for the quarter of the fire and the quarter following the fire, quarters in which it was unable to produce records establishing nontaxable sales, sales invoices, cash register tapes or other source documents relating to its sales and claimed out-of-state sales. In fact, the shipping documents presented to the auditor came from UPS, and were not maintained by petitioners. Thus, for the two sales quarters of and following the fire, petitioners could not provide the Division with any substantiation of the nontaxable sales during the course of the audit, or substantiate their claim at the hearing. This failure to provide documentation of nontaxable sales for the quarters ended May 31, 1987 and August 31, 1987, as required by Tax Law § 1135(a)(1), undermines petitioners' positions that they had nontaxable sales in the audit period and, as well, that they are entitled to have the allowance figure computed for the last quarter applied throughout the audit period. In the absence of evidence that the records for the quarters ended May 31, 1987 and August 31, 1987 were made available to the Division, it is held that the Division's methodology of disallowing all claimed nontaxable sales was reasonable and that no adjustment to the audit is warranted(see, Matter of On the Rox Liqs., Ltd. v. State Tax Commn., 124 AD2d 402, 507 NYS2d 503, lv denied, 69 NY2d 603, 512 NYS2d 1026; Matter of Academy Beer Distributors,

Tax Appeals Tribunal, January 21, 1993; Matter of House of Audio of Lynbrook, supra).

D. Tax Law § 1145(a)(1)(i) authorizes the imposition of a penalty for failure to file a return or to pay any tax under Article 28 in a timely manner. Tax Law § 1145(a)(1)(vi) provides for the imposition of a penalty for the omission from the total amount of sales and use taxes required to be shown on a return an amount which is in excess of twenty-five percent of the amount of such taxes required to be shown on the return. Tax Law § 1145(a)(1)(iii) and (vi) further provide that if the failure, delay or omission was due to reasonable cause and not willful neglect, penalty and that portion of interest which exceeds the minimum amount of interest prescribed by law shall be remitted. In order for the penalties to be abated, the burden is on petitioners to establish reasonable cause as well as the absence of willful neglect.

For the 12 quarters of the audit period and 4 quarters prior thereto, petitioner Tango late filed 3 sales tax returns, filed 8 returns without remittance and filed 4 sales tax returns with a partial remittance. The reason given was the need to use the sales tax trust money to pay other creditors. This cannot be considered reasonable cause.

Petitioner claims that the fire destroyed its records and also made it difficult to maintain records and file returns after the fire. Such may have been the case immediately after the fire but petitioner was unable to produce original source documents for a period of six months after the fire and had no records as to claimed nontaxable sales for the final quarter of the audit until such records were obtained from UPS.

Therefore, petitioners have not met their burden of proof on this case. It is therefore concluded that petitioners were properly held liable for the penalties and interest assessed in this matter.

E. Petitioners request that the penalties imposed be waived because the Division late-filed its answer in this matter. It is undisputed that the Division filed its answer 61 days beyond the 60-day time period prescribed in 20 NYCRR 3000.4(a)(1). However, New York Courts have recognized the general principle that such time periods may be directory rather than mandatory (see, Matter of Geary v. Commr. of Motor Vehicles, 92 AD2d 38, 459 NYS2d 494,

affd 59 NY2d 950, 466 NYS2d 304). Therefore, the Division's latness in answering is not in itself a sufficient basis for granting petitioners' motion (see, Matter of Macbet Realty, Tax Appeals Tribunal, May 17, 1990).

When an administrative agency fails to meet a time constraint established by its own regulations, petitioner must show that the delay resulted in substantial prejudice to its position before a default determination will be awarded (see, e.g., Matter of Cortlandt Nursing Home v. Alexrod, 66 NY2d 169, 495 NYS2d 927, cert denied 476 US 1115; Matter of Maggin, Tax Appeals Tribunal, March 8, 1991). Petitioners have not demonstrated substantial prejudice. In addition, no request was made to schedule these matters for hearing at the time the Division of Taxation served its answer. In sum, there is no basis to default the Division of Taxation because its answer was filed late.

F. The petition of Tango Boutique, Inc. and Rosalind Cook and Judith Lashin, as officers, is denied, and the notices of determination and demands for payment of sales and use taxes due, dated July 5, 1989, as amended by the Bureau of Conciliation and Mediation Services' Conciliation Order and the parties herein, are sustained.

DATED: Troy, New York
May 4, 1993

/s/ Thomas C. Sacca
ADMINISTRATIVE LAW JUDGE