STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
BARRIER MOTOR FUELS, INC.	:	DETERMINATION DTA NO. 816059
for Review of an Increase in the Amount of Bond or Other Security Required to be Filed Under Articles 12-A and 13-A of the Tax Law for the Year 1997.	:	

Petitioner, Barrier Motor Fuels, Inc., P. O. Box 690, 184 West Main Street, Tarrytown, New York 10591, filed a petition for review of an increase in the amount of bond or other security required to be filed under Articles 12-A and 13-A of the Tax Law for the year 1997.

A hearing was held before Roberta Moseley Nero, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on December 4, 1997 at 10:15 A.M. Petitioner's responsive brief was received on March 16, 1998, which date began the six-day period for issuance of this determination.[1] Petitioner appeared by Carl S. Levine & Associates, P.C., (Carl S. Levine, and Diane J. Moffet, Esqs., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (John E. Matthews, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly increased the amount of petitioner's required security from $50,000.00 to $300,000.00, as a condition of maintaining its registration as a New York State diesel motor fuel distributor.

[1]Pursuant to Tax Law § 283(6)(b), an administrative law judge has 15 days from the receipt of the petition to issue a determination in this type of case. The Division of Tax Appeals utilized nine days between the issuance of the Notice of Intent to Dismiss Petition (two days) and scheduling the hearing (seven days). Therefore, six days remain to issue this determination.

FINDINGS OF FACT

1. The Division of Taxation ("Division") issued a notice and demand for an increase in the amount of bond or other security[2] required by Tax Law Articles 12-A and 13-A, in the form of a letter dated August 22, 1997 ("notice") to Barrier Motor Fuels, Inc. The notice increased the amount of petitioner's bond from $50,000.00 to $300,000.00. The explanation of the proposed increase was that an increase was indicated based upon "an analysis of our records and the filing history of Barrier Motor Fuels, Inc." (Division's Exhibit B, Attachment.) The letter also states that the Division had been in contact with a member of petitioner's staff and had been informed by that person that audited financial statements for petitioner would be available around June 9, 1997. The letter states that as of August 22, 1997 no such statements had been received, and that therefore, the amount of the bond required could not be reduced by the net worth of petitioner.

On the second page the notice provides:

> "You have a right to protest this decision within seven (7) days of the date of this letter by written petition, (petition form attached). You must specifically indicate what action of the department you are protesting and attach a copy of this notice to your petition. Send or deliver your petition to:
>
> Supervising Administrative Law Judge
> Division of Tax Appeals
>
> * * *
>
> "Note: You may not request a Conciliation Conference in this case.
>
> "Pursuant to Section 283.6(b)(I)[sic] of the New York State Tax Law, failure to file such increase in the amount of security within such period or to make timely application for a hearing regarding such security increase will result in the cancellation of your diesel motor fuel registration."

2. On September 2, 1997, the Division of Tax Appeals received the petition of Barrier Motor Fuels, Inc. seeking a review of the increase in its bond set forth in the August 22, 1997 notice. The envelope containing the petition bore an office metered mail postmark of August 30, 1997.

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[2]While the Tax Law allows a bond or other security, for purposes of simplification the word bond will be used to refer to bond or other security.

3. On September 4, 1997, the Division of Tax Appeals issued a Notice of Intent to Dismiss Petition which explained that petitioner had seven days from August 22, 1997, the date the notice was issued to file a petition. Since it appeared the petition was filed on August 30, 1997, or eight days later, the Division of Tax Appeals was proposing to dismiss the petition and the parties were given time to submit comments regarding the proposed dismissal. An order was issued on November 19, 1997 determining that the petition was timely filed, withdrawing the Notice of Intent to Dismiss Petition and stating that the matter would be scheduled for hearing not less than five or more than eight days from the issuance of the order. The hearing was scheduled for November 26, 1997, adjourned at the request of petitioner with the consent of the Division, and held on December 4, 1997.

4. The Division's answer in this matter, presumably served on November 21, 1997, stated that petitioner's bond requirement prior to the issuance of the notice was not $50,000.00 as stated in the notice, but was actually $200,000.00. The answer asserted that $150,000.00 of the bond had been applied to a tax liability of petitioner and that the Division was seeking to replace that amount and increase the amount of petitioner's bond by $100,000.00.

5. Testifying on behalf of the Division was Ms. Lois DeFreest. Ms. DeFreest is an Excise Tax Technician II with the Registration and Bond Unit of the Transfer Tax Bureau of the Division. She sent the letter to petitioner that served as the notice in this matter. The tax technician explained that she had done a previous bond computation for this petitioner regarding a different proceeding in 1996. Submitted into evidence was her bond computation worksheet dated June 21, 1996. The tax technician indicated that the bonds petitioner had on file at that time were a $50,000.00 bond put in place in 1990 and a $150,000.00 bond put in place in 1993. She stated that neither of these bonds was calculated regarding any possible Article 13-A liabilities.

6. The Division explained how the bond calculations were done in the present case through

its answer and the testimony of the tax technician. The diesel motor fuel component of the calculation was done as follows:

1) The total gallons of diesel motor fuel from each of the previous six months returns available at the time the computation was done, were taken from petitioner's returns, in particular, PT-102, line 7.

2) Exempt diesel motor fuel sales from each of the previous six months returns available at the time the computation was done, were taken from petitioner's returns, in particular PT-102, lines 8 through 15. The exempt sales were then deducted from the total gallonage to arrive at total taxable gallonage for each of the six months.

3) The Article 12-A tax rate was applied to the total taxable gallonage from each month to arrive at six separate months worth of Article 12-A potential liability. These figures were added together to arrive at a total anticipated six-month potential liability.

4) The applicable sales tax rate was applied to the total taxable gallonage from each month to arrive at six separate months worth of sales tax potential liability. These figures were added together to arrive at a total anticipated six-month potential liability.

5) The Article 13-A automotive tax rate was applied to the total taxable gallonage from each month to arrive at six separate months worth of Article 13-A automotive potential liability. These figures were added together to arrive at a total anticipated six-month potential liability.

6) There were no nonresidential fuel oil sales or Article 13-A nonautomotive gallonage.

7) The calculations done in 1996 had a motor fuel computation done in a similar manner as the diesel motor fuel calculations. The calculations done in July and November 1997 did not contain a motor fuel computation section since petitioner had surrendered its motor fuel licence in 1996.

7. The tax technician explained that the June 21, 1996 computation sheet was done utilizing the months of November 1995 through April 1996 because the information reported by petitioner on its May return was not yet available to her on the computer. The computation included Article 12-A, Article 13-A and Articles 28 and 29 taxes with the following results: a total motor fuel tax of $2,962,067.00; a total diesel motor fuel tax of $338,743.00; and a total due of $3,300,809.00. The computation indicates that certified financial statements were on file with the Division, and that based on those statements 80% of petitioner's equity was computed to be $510,301.00 and this was deducted from the total calculation to arrive at a bond requirement of $2,790,508.00. At the hearing held in the previous matter, petitioner surrendered its motor fuel registration, making this calculation irrelevant.

8. The tax technician indicated that she had been expecting to receive certified financial statements from petitioner sometime in June of 1997. On July 17, 1997 she was informed that the Division's Tax Compliance Division ("TCD") had completed collection against $150,000.00 of the bond petitioner had previously had on file, leaving petitioner with only a $50,000.00 bond. Therefore, she did another bond calculation dated July 17, 1997. This calculation showed zero potential liability for motor fuel sales since petitioner had turned in its motor fuel registration. For diesel motor fuel the computation showed the following: 12-A potential liability of $81,044.00; sales tax potential liability of $82,057.00; 13-A automotive liability of $145,372.00; for a total potential liability of $308,473.00. The computation indicated that audited financial statements were not on file and therefore, no deductions were made for petitioner's total equity. The total bond requirement was $308,473.00, and this was the basis for the notice issued in this matter.

9. The parties stipulated on the record at the hearing that petitioner buys all of its product in State and tax-paid. The Division's representative stated that petitioner had a history of having no diesel fuel tax liability because of this, and in fact petitioner often generated credits because of exempt sales. All of the gallonage used in calculating the bond was purchased by petitioner in State and tax-paid.

10. Petitioner introduced into evidence various articles of correspondence between petitioner and TCD, together with five mortgages of five different properties listing the New York State Department of Taxation and Finance as mortgagee. Each mortgage provides that it is to secure an indebtedness in the amount of $2,325,000.00 which the various mortgagors agree to pay in accordance with the terms of a deferred payment agreement between the Division and petitioner. The mortgages are for a total amount of $1,400,000.00. Petitioner's representative explained at hearing that there had been a mistake and that the deferred payment agreement had not been signed. Petitioner was given until December 19, 1997 to submit a copy of the signed deferred payment agreement. No agreement was submitted. The correspondence submitted by petitioner indicates that there were discussions and an apparent agreement regarding a deferred

payment agreement between petitioner and the TCD. A letter dated November 26, 1996 from Mr. Daniel F. Malone, Director, District Office Compliance Bureau, TCD, summarizes such an agreement by indicating that petitioner's liability was approximately $1,500,000.00, prior to applying the $150,000.00 from the security. It further states that petitioner is offering $1,400,000.00 in security for the agreement (the mortgages) and concludes by stating that it is important that the documentation provided by petitioner concerning the securities confirms this.

11. The Division was allowed until December 29, 1997 to submit its response to any deferred payment agreement submitted by petitioner and to petitioner's exhibits which had not been seen by the Division's representative prior to the hearing. There was no deferred payment agreement submitted by petitioner, but the Division did submit the affidavit of Mr. Theodore Eckler in response to petitioner's exhibits. Mr. Eckler is a Tax Compliance Agent II, employed in TCD, whose duties include reviewing real property mortgages relevant to deferred payment agreements. Mr. Eckler's knowledge of this case is from reviewing the file and being personally involved in the case. His affidavit confirms the information set forth in petitioner's exhibits that the security supported by the mortgages totaled $1,400,000.00 (i.e., appraised value of the mortgaged properties less liabilities). He also stated that petitioner's outstanding tax liabilities totaled approximately $2,121,940.00 as of the December 23, 1997 execution of his affidavit. The affidavit does not attempt to explain the difference in the amounts of tax liabilities as related by Mr. Malone ($1,500,000.00, prior to applying the $150,000.00 from the bond, and his figure of $2,121,940.00 after applying the $150,000.00 from the bond). It is possible that since there are approximately 13 months between Mr. Malone's letter and Mr. Eckler's affidavit that the approximately $750,000.00 difference is attributable to interest.

12. The parties originally had until January 22, 1998 to file simultaneous briefs and until February 12, 1998 to file responsive briefs. The Division's original brief was received on January 21, 1998. Petitioner did not file a brief. Since petitioner had not filed a brief, it was unnecessary for the Division to file a responsive brief. Through several extensions, petitioner's responsive brief was due and filed on March 13, 1998 and received on March 16, 1998. Much of

petitioner's brief appears to be in the nature of a brief in support of its petition. However, since petitioner's arguments in support of its petition and in opposition to the Division's notice are difficult to separate in this matter, and since the arguments presented conform with those presented at the hearing, and the Division has not raised an objection, petitioner's brief is accepted.

SUMMARY OF THE PARTIES' POSITIONS

13. The petition states that the Division's decision to increase the amount of petitioner's required security was unjustified under the law and regulations, and was arbitrary, capricious and an abuse of discretion. The petition also states that petitioner's due process rights were violated in that the notice did not provide petitioner with sufficient information to enable the petitioner to respond to it.

Petitioner argues that it was improper for the Division to not take into account its tax-paid purchases when calculating the proposed increase in its bond. In particular petitioner points out that the calculation as done by the Division does not reflect petitioner's potential tax liability as required by the regulation since petitioner purchases all of its product tax paid and therefore has no potential tax liability. Finally, petitioner argues that it has already provided the Division with sufficient security.

14. The Division argues that the $1,400,000.00 in mortgage security has specifically been pledged to secure certain outstanding tax liabilities and therefore is not available for use as security in insuring payment of future liabilities. Also, the Division argues that the mortgages are not even available to it since they are dependent upon the terms of the deferred payment agreement which petitioner did not introduce into the record. The Division asserts that even if the agreement been submitted and the $1,400,000.00 had been available to satisfy future liabilities, since it was less than the value of the outstanding liabilities, there would not have been any value to apply to future liabilities. On the issue of giving petitioner credit for tax-paid purchases the Division argues that there is no provision in the statute or regulation that allows the Division to do this. The Division points out that, while the regulations governing motor fuel bonding provide

for credit for tax-paid purchases, and the statute dealing with diesel motor fuel bonding provides that tax exempt gallons be subtracted out in calculating bond amounts, there is no provision in the statute or the regulation allowing for the subtracting out of tax-paid product when calculating the amount of a diesel motor fuel bond. The Division asserts that at some time in the future petitioner could either purchase product tax free from out of State or home heating oil tax-free in State and sell it as diesel motor fuel, and that since either of these actions could result in petitioner's accruing future tax liabilities in an amount equal to the calculation, that it is entitled to require a bond in this amount.

CONCLUSIONS OF LAW

A. Article 12-A of the Tax Law imposes a tax on gasoline and similar motor fuel. Tax Law § 283(3) requires the registration of distributors, and requires distributors to file a bond as follows:

> "The tax commission shall require a distributor to file with the department of taxation and finance a bond issued by a surety company approved by the superintendent of insurance as to solvency and responsibility and authorized to transact business in this state or other security acceptable to the tax commission, in such amount as the tax commission may fix, in an amount determined in accordance with rules and regulations prescribed by it, to secure the payment of any sums due from such distributor (i) pursuant to this article and (ii) pursuant to articles twenty-eight and twenty-nine of this chapter with respect to sales and uses of motor fuel. The tax commission shall require that such a bond or other security be filed before a distributor is registered, and *the amount thereof may be increased at any time when in its judgment the same is necessary as a protection to the revenues under this article and under articles twenty-eight and twenty-nine of this chapter*."[3] (Tax Law § 283[3]; emphasis added.)

Tax Law § 282-a imposes an excise tax upon the sale or use of diesel motor fuel. The procedural provisions regarding determining or increasing the amount of a bond for motor fuel apply to diesel motor fuel (Tax Law §282-a[5]).

Article 13-A of the Tax Law imposes a tax on petroleum businesses. Tax Law § 302(c) describes the various forms of registration required by Article 13-A, and requires petroleum

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[3]Pursuant to Tax Law § 2(1) "tax commission" as used in this subdivision is to be interpreted as referring to the Commissioner of Taxation and Finance.

businesses to file a bond as follows:

> "The commissioner may require a petroleum business to file with it a bond issued by a surety company approved by the superintendent of insurance as to solvency and responsibility and authorized to transact business in this state or other security acceptable to the commissioner, in such amount as the commissioner may fix in an amount determined in accordance with rules and regulations prescribed by the commissioner, to secure the payment of any sums due from such petroleum business pursuant to this article. The commissioner may require that such a bond or other security be filed before a petroleum business is registered, and *the amount thereof may be increased at any time when in the commissioner's judgment the same is necessary as a protection to the revenues under this article*." (Tax Law § 302[c]; emphasis added.)

The procedural provisions regarding increasing the amount of a bond found in Article 12-A apply also to Article 13-A (***see***, Tax Law § 302[c]; § 315[a],[b]).

Pursuant to these provisions the Division determined to increase the amount of petitioner's bond and issued a notice and demand for the new amount of $300,000.00. The question presented is whether the Division correctly calculated the amount of the increased bond. Based on the record and the arguments presented, it was unreasonable for the Division to calculate the amount of petitioner's bond without taking into consideration the fact that the gallonage used to calculate the amount of the bond was purchased tax-paid.

B. The purpose of the bonding requirements is to protect the revenues of the State of New York by securing payment of motor fuel, diesel motor fuel and petroleum business taxes (***see***, ***Matter of Certified Heating Oils***, Tax Appeals Tribunal, November 15, 1990, citing ***Matter of Major Oils***, Tax Appeals Tribunal, August 4, 1988). The mechanism for determining the amount of bond to be required for distributors of motor fuel under Tax Law Article 12-A is found in 20 NYCRR 411.2(b), which provides:

> "(1) Prior to the approval of an application for registration as a distributor of motor fuel and during any subsequent review of a registered distributor, the Department of Taxation and Finance, in determining the amount or sufficiency of a bond, will:
>
> "(i) determine the estimated or representative six-month maximum potential tax liability of the applicant or of the distributor (see paragraph [2] of this subdivision);
>
> "(ii) analyze the certified financial statements of the applicant or distributor with particular emphasis on the ratio of current assets to current

liabilities and net worth (total assets less total liabilities) as determined in accordance with generally accepted accounting principles;

"(iii) review the taxpayer's compliance record to determine whether there are or were any delinquencies in filing returns and/or payment of any taxes as a distributor of motor fuel or any other taxes due New York State for which the applicant or distributor may be or may have been responsible.

"(2) For purposes of this section, maximum potential liability is determined based on an anticipated total number of gallons of motor fuel expected to be imported into the State or produced, refined, manufactured, compounded, sold, transferred, used or otherwise distributed within New York State by the applicant or based on a representative total number of gallons of motor fuel imported into the State or produced, refined, manufactured, compounded, sold transferred, used or otherwise distributed within New York State by the distributor, without any reductions for those gallons subject to tax-free or exempt sales. Generally, in determining the amount of such representative or anticipated total gallonage, the department shall, based on a prior consistent business practice of the applicant or distributor, consider those gallons of motor fuel purchased and/or reasonably expected to be purchased within the State on which the taxes on motor fuel pursuant to Articles 12-A, 28 and 29 of the Tax Law have been or will be assumed or paid by another distributor of motor fuel snd[sic] included in such purchase price, as evidenced by certifications of tax payment. (See sections 412.3 and 412.4 of this Title for certifications.) The number of gallons of motor fuel determined is multiplied by the rate of the motor fuel tax per gallon and by the applicable rate (see section 561.3[b] of this Title) of the prepaid sales tax per gallon. The sum of these taxes shall then be adjusted where necessary to reflect a six-month tax liability.

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"(3)(v)(*a*) . . . generally the amount of a bond required to be filed and maintained pursuant to the provisions of this section shall not be less than $50,000.

* * *

"(*b*) Provided further, generally the amount of a bond shall not exceed the six-month maximum potential tax liability of the applicant or of the distributor except to the extent such six-month maximum potential tax liability is less than $50,000.

* * *

"(vii) . . . the amount of a bond may be adjusted where any information indicates the need for a bond in greater or lesser amount."

There are no specific regulations that set forth how to calculate the amount of a bond for diesel motor fuel distributors under Article 12-A. Furthermore, there are no regulations adopted under the authority of Article 13-A in general, nor are there any regulations specifically detailing

the method for determining the amount of a bond required under Article 13-A. However, under the general statutory scheme that provides for the administrative and procedural requirements that apply to Article 12-A motor fuel distributors to also apply to Article 12-A diesel motor fuel distributors and Article 13-A petroleum businesses (***see***, Tax Law § 282-a[5]; § 302[c]; § 315[a],[b]), it was proper for the Division to utilize 20 NYCRR 411.2 to determine the amount of bond required from petitioner. This statutory scheme has several exceptions. First, under Article 12-A, the provisions regarding motor fuel distributors are to be applied to diesel motor fuel distributors "with such modification as may be necessary to adapt the language of such provisions" (Tax Law § 282-a[5]) to the diesel motor fuel situation. Second, Article 12-A motor fuel provisions apply to Article 13-A petroleum businesses "except to the extent that any such provision is either inconsistent with or not relevant to" (Tax Law § 315[a]) the petroleum business tax. Finally, when calculating the amount of a bond for diesel motor fuel:

> "the commissioner of taxation and finance . . . shall take into account the volume of heating fuel and other Diesel motor fuel sold for exempt purposes by a distributor of Diesel motor fuel during prior periods as a factor reducing potential tax liability along with any other relevant factors in determining the amount of security required." (Tax Law § 282-a[5].)

C. Where, as in this case, no certified financial statements were provided to the Division, the Division calculates the amount of a bond by determining a distributor's maximum six-month tax liability. In the case of diesel motor fuel any exempt sales are deducted from this number to arrive at the anticipated number of gallons to be sold. This number is multiplied by the appropriate tax rate or rates to determine the anticipated maximum liability. In this case the gallonage was multiplied by the appropriate rates for diesel motor fuel, sales and petroleum business taxes. As evidenced by the audit workpapers, and the testimony of the tax technician, the Division performed theses calculations correctly and in accordance with 20 NYCRR 411.2.

However, petitioner argues that since the gallonage utilized by the Division in calculating the amount of the bond was purchased tax-paid, those gallons should also be subtracted prior to applying the tax rates. In this case, since the Division admits that all of this product was purchased tax-paid, the required security would equal zero.

The tax technician testified that she deducted exempt sale gallonage because that is what the statute said and she did not deduct tax-paid product because the statute did not direct her to do so. This testimony conforms with the legal arguments presented by the Division in its brief. It is correct that Tax Law § 282-a(5) requires the Division to subtract exempt sale gallonage when calculating diesel motor fuel bonds. It is also true that the statute is silent regarding tax-paid product when calculating such bonds. However, there is no statutory provision requiring the Division to deduct tax-paid product in calculating the amount of a bond for either motor or diesel motor fuel bonds. The basis for deducting tax-paid product in the motor fuel area is 20 NYCRR 411.2 (2).

As noted above 20 NYCRR 411.2, while referring to motor fuel sales, is properly applied in calculating the amount of diesel motor fuel and petroleum business tax bonds. The Division has not presented any argument that the deducting of tax-paid product in its bond calculation is somehow inconsistent with the statutory provisions governing either diesel motor fuel or petroleum business tax. Therefore, there is simply no basis not to apply the particular provisions of 20 NYCRR 411.2(2) and deduct the tax-paid product in calculating petitioner's bond.

The Division argues that petitioner could in the future purchase diesel motor fuel tax free out of State or purchase product labeled home heating oil and then sell it as diesel motor fuel. These actions on the part of petitioner could produce a tax liability approximating that calculated by the Division. However, the Division does not explain how this possible action of petitioner, which would be a total change from petitioner's past practices, requires that 20 NYCRR 411.2(2) be ignored in calculating petitioner's bond. Furthermore, the formula utilized to calculate anticipated tax liability utilizes past experience. The past experience with petitioner is that it has not owed any diesel motor fuel tax, and has actually generated credits because of exempt sales, because it purchased its product tax-paid. Under these circumstances it is not reasonable for the Division to ignore the regulation and base the calculation of petitioner's bond on an unforseen future event contrary to the past business practices of petitioner.

D. The provisions governing bonds for Article 12-A diesel motor fuel and Article 13-A

petroleum business tax do not require that there be a minimum bond (Tax Law § 282-a[5]; § 302[c]), as required by Tax Law § 283(3) for Article 12-A motor fuel tax. However, petitioner has not requested that the $50,000.00 bond currently on file with the Division be eliminated. Furthermore, taking into account petitioner's other current outstanding tax liabilities (***see,*** 20 NYCRR 411.2[b][1][iii]), it is reasonable to require the bond of $50,000.00.

E. Petitioner did not raise the arguments presented in the petition regarding lack of adequate notice either at the hearing or in its brief. Therefore, those arguments are considered abandoned and will not be addressed. The arguments presented by the parties on the issue of whether the mortgages provided to the Division to secure a deferred payment agreement on outstanding tax liabilities could be used as security in a bonding situation, are rendered moot by the determination that petitioner's bond will not be increased.

F. The petition of Barrier Motor Fuels, Inc. is granted and the notice and demand for an increase in the amount of bond or other security, in the form of a letter dated August 22, 1997, is canceled.

DATED: Troy, New York
March 19, 1998

/s/ Roberta Moseley Nero
ADMINISTRATIVE LAW JUDGE