

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
IHAB M. HILWEH : DETERMINATION
D/B/A ALBANY RESTAURANT SUPPLY : DTA NO. 818465
: :
for Revision of a Determination or for Refund of Sales and :
Use Taxes under Articles 28 and 29 of the Tax Law for the :
Period June 1, 1994 through May 31, 1997. :
:

Petitioner, Ihab M. Hilweh d/b/a Albany Restaurant Supply, 7 Interstate Avenue, Albany, New York 12205, 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 June 1, 1994 through May 31, 1997.

A hearing was held before Jean Corigliano, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York on February 14, 2002 at 1:30 P.M., with briefs to be submitted by June 20, 2002, which date began the six-month period for the issuance of this determination. Petitioner appeared by David L. Evans, C.P.A. The Division of Taxation appeared by Barbara G. Billet, Esq. (Michael P. McKinley, Esq., of counsel).

ISSUES

- I. Whether petitioner maintained adequate books and records of sales.
- II. Whether petitioner has established that the audit method used by the Division of Taxation was unreasonable or that the results of the audit were incorrect.

FINDINGS OF FACT

1. As a result of a sales tax field audit, the Division of Taxation (“Division”) issued to petitioner, Ihab M. Hilweh d/b/a Albany Restaurant Supply, a Notice of Determination, dated January 22, 1999, assessing sales and use taxes due of \$167,791.57 plus interest for the period June 1, 1994 through May 31, 1997.¹

2. Petitioner sells new and used restaurant supplies and equipment. Petitioner's facility includes a warehouse, offices and a retail showroom. The Division initiated an audit because a review of petitioner's sales tax returns showed an unusually low ratio of taxable sales to gross sales compared with similar businesses. Petitioner reported taxable sales of approximately 20 percent of gross sales for the audit period.

3. An audit appointment letter, dated June 6, 1997, was sent to petitioner informing him that a field audit had been scheduled for the period June 1, 1994 through May 31, 1997. Petitioner was asked to make all of the books and records pertaining to the company's sales tax liability available at the time of the audit. Among other things, petitioner was asked to provide financial statements, journals, ledgers, sales invoices, purchase invoices, cash register tapes, tax returns and exemption certificates.

4. On July 21, 1997, the auditor visited the business premises where he took a tour of the facilities and discussed the impending audit with petitioner. The auditor determined that petitioner did not have a sales journal, a cash receipts journal or a purchase journal available for audit. Moreover, he found that petitioner's sales invoices were not maintained in a manner that would allow him to verify petitioner's gross sales for the audit period. This was because the sales

¹ Mr. Hilweh signed a series of consents ultimately extending the period of limitation for assessment of sales and use taxes due for the period June 1, 1994 through February 29, 1996 to March 20, 1999.

invoices were filed alphabetically in individual folders by customer name. The folders might contain several invoices and exemption certificates from a period of years. Since the invoices were not maintained in chronological order, or in numerical order by invoice number, and petitioner did not maintain a sales ledger where each individual sale would be posted, the auditor could not determine whether all invoices for the audit period were available even if he pulled invoices from the folders and attempted to organize them chronologically.

5. Petitioner's bookkeeper informed the auditor that petitioner determined gross sales for tax and financial purposes by reference to the company's bank deposits which included check, cash and credit card deposits. Since petitioner made few cash payments, the auditor concluded that petitioner's bank deposits would provide a fairly accurate statement of petitioner's gross sales.

6. The auditor conducted a test period audit for the period March 1, 1997 through May 31, 1997. He requested, and was given, bank statements and bank deposit slips for this period. He also asked for a listing of all nontaxable items included in the bank deposits and verification that the nontaxable items should not be included in taxable sales. The auditor's workpapers include a copy of the business bank statements he relied on. They show, among other things: direct deposits from cash sales and credit card sales; checks issued; withdrawals; stop payments; and fees. From these statements, the auditor computed audited gross sales of \$691,616.00 for the test period. This compares with gross sales reported by petitioner of \$683,682.00. The auditor asked petitioner to present evidence of any nontaxable sales included in audited gross sales. Petitioner presented the auditor with invoices, tax exempt certificates and other documents to substantiate his claimed nontaxable sales. On audit, petitioner claimed exempt sales of \$98,005.30. Of this amount, the auditor was able to verify sales for resale or sales to exempt organizations in the

amount of \$94,581.68. The work papers contain a listing of each claimed exempt sale, by purchaser's name, the amount of the sale and an indication of whether a tax exempt certificate or some other indication of nontaxable status was presented. The auditor was also able to verify out-of-state sales of \$17,554.70; returned merchandise representing \$18,575.64 in sales; redeposited checks of \$10,832.22; cash deposits on purchases of \$42,500.00; leases of \$8,700.00; the difference between the 8 and 7 percent sales tax on sales located outside of Albany County; and sales tax collected. Total nontaxable sales were determined to be \$204,366.01. The difference between gross sales and verified nontaxable sales was \$487,249.22. Petitioner reported taxable sales for the audit period of \$143,570.00. Thus, additional taxable sales were determined to be \$343,679.99. The additional taxable sales were divided by total sales reported by petitioner (\$683,682.00) to compute an error rate of 50.27 percent. The error rate was applied to petitioner's reported gross sales for the audit period (\$4,517,899.00) to calculate additional taxable sales of \$2,271,101.89 with a tax due of \$181,688.15.

7. The auditor discussed the audit results with Mr. Hilweh and his sister, who was then the company's bookkeeper. Petitioner was dissatisfied with the audit results. At the auditor's suggestion, petitioner agreed to a second test period audit. Mr. Hilweh signed a Test Period Audit Method Election form, dated October 8, 1998, agreeing to allow the Division to perform a test period audit of sales and recurring expense purchases. The following statement appears at the bottom of the form: "This form is to be used during the course of a tax audit to provide a taxpayer the option of a test period audit method where a detailed or statistical sampling method audit may be possible."

8. A second test period audit was conducted using the same methodology as was used on the first test. The period tested was September 1, 1996 through November 30, 1996 and resulted

in an error rate of 40.54 percent. The auditor then combined the two test quarters to calculate an error rate of 46.42 percent for the audit period. Application of this error rate to gross sales reported for the audit period resulted in additional taxable sales of \$2,097,395.04 with a tax due on that amount of \$167,791.60.

9. Petitioner was represented on audit by an accountant, Salvatore Iavarone. It appears from the auditor's log that most of his contacts were with Mr. Hilweh and his sister; however, the auditor discussed the audit results with both Mr. Hilweh and Mr. Iavarone.

10. To prove the incorrectness of the audit results, petitioner attempted to duplicate the audit for the two test periods, using all the sales invoices, exempt certificates and other records its new bookkeeper, Katherine Ferguson, was able to gather over a period of several months. Although she eventually located all, or almost all, of the relevant documentation, she encountered some difficulty with this task because the invoices were disorganized and filed in a fashion which she described as "random." Moreover, several invoice pads were used to write sales, so the invoices could not be arranged in numerical order. Bank statements, sales invoices, tax exempt certificates and resale certificates were placed in evidence. Many of the invoices and tax exempt certificates correspond to the auditor's listing of substantiated nontaxable sales.

11. Using the documentation gathered by Ms. Ferguson, petitioner's hearing representatives calculated petitioner's taxable sales for the two test periods, using the same methodology that had been used by the auditor. A summary of the results and a comparison of petitioner's own audit results with those of the Division was also prepared. The comparisons as calculated by petitioner are as follows:

September 1,1996 - November 30, 1996

	Petitioner	Division
Gross Sales:	\$ 463,656.19	\$ 463,656.19
Less:		
Tax Exempt Sales:	127,250.58	120,357.94
Out-of-State Sales:	3,454.34	1,948.77
Returns:	28,126.58	18,188.98
Deposits:	21,714.00	21,714.00
Lease:	15,500.00	21,360.00
Sales Tax Collected:	7,328.16	7,328.16
Total Non-Taxable Sales:	203,373.66	190,897.85
Additional Taxable Sales:	168,680.53	181,156.34

March 1, 1997 through May 31,1997

Gross Sales:	\$ 691,616.00	\$ 691,616.00
Less:		
Tax Exempt Sales:	102,728.27	94,581.68
Out-of-State Sales:	27,110.14	17,554.70
Returns:	18,619.51	18,575.64
Redeposited Checks:	10,832.22	10,832.22
Deposits:	42,500.00	42,500.00
Lease:	8,700.00	8,700.00
8% Amount	136.77	136.77
Sales Tax Collected:	11,465.00	11,465.00
Total Non-Taxable Sales:	222,111.91	204,366.01
Additional Taxable Sales:	325,934.09	343,679.99

SUMMARY OF THE PARTIES' POSITIONS

12. Petitioner maintains that he kept adequate books and records and was entitled to a detailed audit of the books and records. Inasmuch as a test period audit was conducted, petitioner argues that the assessment should be canceled or reduced.

13. Petitioner maintains that the majority of his sales were made to out-of-state purchasers and were exempt from New York State sales tax. He claims that the auditor disallowed a high number of petitioner's exempt sales without allowing him an opportunity to produce invoices or exemption certificates to show that sales were tax exempt.

14. Petitioner argues that the Division could have arrived at more accurate results if it had used a more accurate audit method such as a statistical sampling methodology. Moreover, petitioner notes that mistakes were made by the auditor and asks that the assessment be lowered as a consequence.

15. Petitioner's wife testified that petitioner is a salesman and not familiar with record keeping and other financial matters. She stated that he becomes nervous and uncomfortable when presented with accounting matters.

16. The Division notes that Mr. Hilweh executed a Test Period Audit Method Election form enabling the Division to perform a test period audit. It argues that petitioner has not shown that the audit method used was unreasonable or that the results were inaccurate. It claims that petitioner's failure to provide evidence of a substantial amount of nontaxable sales is evidence that petitioner realizes that the Division's test period audit results are representative.

17. The Division asks that audit errors made in petitioner's favor be considered in determining whether the audit results should be adjusted. For both test periods, the auditor subtracted cash deposits from gross sales. Since petitioner is a cash basis taxpayer, all amounts received within a test period should have been included in gross sales including deposits on sales where the balance of the amount due was received after the test period. If cash deposits had been included, the assessment would have been \$20,514.45 higher.

CONCLUSIONS OF LAW

A. Once a notice of determination is issued, the burden of proof is on petitioner to demonstrate that the basis for the assessment is unreasonable or that the amount of tax assessed is incorrect (*Matter of Micheli Contracting Corp. v. New York State Tax Commn.*, 109 AD2d 957, 486 NYS2d 448; *Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451, 452). Here, petitioner has failed to establish any grounds for canceling or adjusting the Notice of Determination issued to him.

B. Petitioner's books and records were inadequate for the purpose of performing a detailed audit. "Every person required to collect tax shall keep records of every sale . . . and of all amounts paid, charged or due thereon and of the tax payable thereon, *in such form as the commissioner of taxation and finance may by regulation require*" (Tax Law §1135[a][1], emphasis added). By regulation, the Commission requires that all records of sales, including sales invoices, "must be dated, legible, and maintained and preserved in such manner as to disclose in readily accessible and verifiable detail the basis for and accuracy of the entries reported on the sales and use tax return" (20 NYCRR 533.2[f][1][i]). Petitioner's sales invoices were not maintained in a readily accessible manner. His witness described the business's filing practices as disorganized and "random." The invoices were not filed chronologically or by invoice number. More than one set of invoice forms were used during a single time period so the invoices could not be arranged numerically. The invoices were kept in customer invoice folders with several years worth of invoices in one folder. The Division's auditor was not required to organize these invoices in order to determine whether petitioner had a complete set of invoices for the audit period; rather, the burden was on the taxpayer to maintain the invoices in an accessible manner and to provide the auditor with an organized set of invoices. Since

petitioner's books and records were inadequate to permit an exact computation of the sales and use taxes due, the Division was authorized to estimate petitioner's tax liability using any audit methodology reasonably calculated to reflect the taxes due (Tax Law § 1138[a][1]; *see, Matter of Ristorante Puglia, Ltd. v. Chu*, 102 AD2d 348, 478 NYS2d 91).

C. There is no evidence to show that the audit method selected by the auditor was unreasonable. The auditor accepted petitioner's method of calculating gross sales and used it to determine gross sales for each of the test periods and for the entire audit period. Accordingly, petitioner has not established that the Division inaccurately calculated gross sales for the audit period.

Petitioner has shown no error in the Division's use of a test period audit. For example, petitioner has not argued that the test periods were not representative of petitioner's business. Moreover, Mr. Hilweh executed a Test Period Audit Method Election form allowing the Division to conduct a test period audit to determine his tax liability. Evidence that Mr. Hilweh is not comfortable with accounting matters does not create grounds for disregarding the election form. He is the owner of the company, he discussed the audit with the auditor, and he was represented by an accountant. There is no evidence that would justify nullification of the election form.

To determine taxable sales, the auditor presumed that all sales of tangible personal property were subject to sales tax and allowed petitioner to present evidence of the nontaxable status of individual sales. He then accepted all evidence offered to him to substantiate nontaxable sales. Both the presumption of taxability and the placing of the burden of proof on the taxpayer to establish any nontaxable sales was required by Tax Law § 1132(c). Petitioner failed to show that this audit method was unreasonable.

Petitioner's claim that a statistical sampling methodology would have yielded more accurate results has no merit. A taxpayer cannot meet his obligation to prove by clear and convincing evidence that an audit method was unreasonable or the results inaccurate merely by arguing that a different method would have yielded more accurate results (*see, Matter of Scholastic Specialty Corp. v. Tax Appeals Tribunal*, 198 AD2d 84, 603 NYS2d 357 *lv denied* 83 NY2d 751, 611 NYS2d 133; *Matter of Shukry v. Tax Appeals Tribunal*, 184 AD2d 874, 585 NYS2d 531).

D. The evidence presented by petitioner at hearing provides no grounds for reducing or canceling the assessment. Petitioner's evidence of nontaxable sales in the two test periods reduces the calculation of additional taxable sales for the two periods combined to \$494,614.62 (the Division calculated additional taxable sales for the two periods of \$524,836.33). However, if cash deposits of \$64,214.00 are added to petitioner's calculation to accurately reflect the evidence in the record, total additional taxable sales amount to \$558,828.00, which increases petitioner's tax liability. In addition, petitioner had no records to substantiate points of delivery for claimed out-of-state sales as required by the regulations (20 NYCRR 533.2[b][3]). In short, he merely substituted his own estimate of tax due for the Division's using the Division's calculations as a starting point. It is telling that petitioner's estimate of unreported taxable sales for the two test periods is \$494,614.62. Petitioner never offered an explanation for the large discrepancy between his reported taxable sales and the taxable sales shown in his own records. Petitioner's proof falls short of showing the incorrectness of the audit by a standard of clear and convincing evidence.

E. The petition of Ihab M. Hilweh d/b/a Albany Restaurant Supply is denied and the Notice of Determination, dated January 22, 1999 is sustained.

DATED: Troy, New York
September 26, 2002

/s/ Jean Corigliano
ADMINISTRATIVE LAW JUDGE