STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
STRAIGHT PATH SERVICE STATION, INC.	:	
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 December 1, 1999 through November 30, 2004.	:	DETERMINATION DTA NO. 821621

Petitioner, Straight Path Service Station, Inc., filed a petition for revision of a determination or refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1999 through November 30, 2004.

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on December 19 and 20, 2007, with all briefs due by July 7, 2008, which date began the six-month period for the issuance of this determination. Petitioner appeared by David L. Silverman, Esq. The Division of Taxation appeared by Daniel Smirlock, Esq. (Osborne K. Jack, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation properly resorted to an estimated audit methodology to determine petitioner's sales and use tax liability for the period in issue.

II. Whether the Division of Taxation, using the gallons sold in determining petitioner's additional sales tax liability, properly determined the correct prepaid gasoline tax credit and the resultant additional sales tax due.

III. Whether petitioner has demonstrated reasonable cause for the abatement of penalties asserted by the Division of Taxation pursuant to Tax Law § 1145.

FINDINGS OF FACT

1. During the period December 1, 1999 through November 30, 2004 (the period in issue), petitioner operated service stations in Franklin Square, Huntington Station and West Babylon, New York, making sales of gasoline, diesel fuel, cigarettes, and miscellaneous convenience store items. Only the West Babylon location had a mini market, while the other locations sold merchandise from booths located near the gasoline pumps.

2. The Division of Taxation began its audit of petitioner on October 4, 2002, when it mailed petitioner an appointment letter and a request for books and records for the period December 1, 1999 through August 31, 2002 with respect to petitioner's sales and use tax liability. The letter specifically requested all books and records pertaining to sales and use tax liability and made reference to a detailed list of records it wished to examine at the appointment. The letter also stated that additional records and information might be requested.

3. The "records requested list" attached to the October 4, 2002 letter included the following documents and information for the entire audit period: sales tax returns; worksheets and cancelled checks ; federal income tax returns; New York State corporation tax returns; the general ledger; general journal and closing entries for the entire audit period; sales invoices; exemption documents; chart of accounts; fixed asset purchase and sales invoices; expense purchase invoices; merchandise purchase invoices; bank statements, canceled checks and deposit slips; cash receipts journal; cash disbursement journal; corporate book; financial statements; power of attorney; depreciation schedules; other locations and their respective functions. At no

time during the pendency of the audit of petitioner were all of these records produced at one time for inspection.

4. The first auditor assigned to the case, Jennifer D. Buscemi, contacted petitioner's representative, Steven Schneiderman, CPA, and arranged to meet him at his office on November 27, 2002. At that time, she was presented only with copies of the federal income tax returns for the audit period, sales and use tax returns and related schedules and worksheets for the period March 2001 through August 2002, the year-end trial balances for 2001 and 2002 and purchases as demonstrated by check disbursements. It was not disclosed in the record when petitioner or its representative informed the Division that it maintained no original source documentation for its sales of gasoline, diesel or kerosene. However, Mr. Schneiderman told Ms. Buscemi that he did not have the records requested available for inspection and that producing them would have been too voluminous and "almost impossible." Further, since petitioner maintained no source documentation of its sales, there was no documentation of sales produced for the first meeting with the auditor. Mr. Schneiderman never had records for the first seven months of the audit period to offer the Division.

5. Utilizing the information supplied by Mr. Schneiderman at the November 27, 2002 meeting, the auditor analyzed gross sales and attempted a purchases reconciliation for the years 2001 and 2002. After finding additional missing information, Ms. Buscemi made an additional request for records from Mr. Schneiderman by letter, dated January 9, 2003. Ms. Buscemi requested copies of the sales and use tax returns for the period December 1, 1999 through February 28, 2001, the 1999 and 2000 income statements, invoices for fixed assets purchased during the audit period, three months of purchases paid for by check for the period March 1,

2002 through May 31, 2002 (the test period) and six months of cash purchases as listed on petitioner's sales tax return worksheets for the period March 1, 2002 through August 31, 2002.

6. As noted, petitioner maintained no original source documentation for sales, such as cash register tapes, sales invoices or cash receipts journals, and instead it filed its sales tax returns for the period in issue on the basis of purchases of petroleum products. Although the opening and ending inventory amounts were available to petitioner, only purchase information was used to estimate sales, while opening and ending inventory amounts were assumed to be equal and inconsequential over time. This created a discrepancy between the gallons petitioner determined to be sales and sales calculated by the Division, which utilized petitioner's inventory figures, purchases and pump prices to arrive at the monthly and quarterly sales during the test period.

7. A subsequent meeting took place between Ms. Buscemi and Mr. Schneiderman on May 21, 2003, at which the auditor received missing sales tax return information and gas purchase invoices for March through May of 2002. The auditor also transcribed cash purchase information for the months of June and July, 2002.

8. Sometime prior to February 26, 2004, the audit file was reassigned to a second auditor, Robert DeFillippis, who informed Mr. Schneiderman by letter of June 9, 2005, that the audit period was being expanded to include the period September 1, 2002 through November 30, 2004 and that all books and records pertinent to petitioner's sales and use tax liability for the updated period should be available for review at the next appointment. The records requested were set forth on a separate sheet and included cash register tapes, sales invoices and sales receipts journals and other records included with the original appointment letter of October 4, 2002. Again, no original source documentation of sales was produced by petitioner.

9. The Division met Mr. Schneiderman at his office on June 15, 2004 and reviewed purchase invoices, schedules and petitioner's method of preparing its sales tax returns. Based on this information and average selling prices for gas stations in petitioner's geographic area, the Division began an analysis of petitioner's sales tax return worksheets. After a year of further investigation, the Division completed its corrected sales tax return worksheets for March through May 2002, compared them with petitioner's worksheets and determined error ratios and the resulting additional sales tax due on sales of petroleum products. Additionally, the Division utilized third party information to confirm convenience store sales, sales tax on convenience store sales and prepaid cigarette tax.

10. After meetings with petitioner on June 10 and October 14, 2005, the Division received additional documentation of average prices per gallon of gasoline sold during the test period of March through May 2002, prepaid gasoline tax, diesel invoices for March 2002 and a reconciliation of gas and diesel purchases during the test quarter. Mr. DeFilippis told Mr. Schneiderman that the books and records petitioner had produced were insufficient to substantiate the tax reported on petitioner's returns under audit, a conclusion which Mr. Schneiderman conceded the auditor had reached and unequivocally communicated to him.

11. Using information supplied by petitioner, the Division took opening inventory, added purchases and subtracted closing inventory to arrive at net purchases, which were deemed total gallons sold. This figure was multiplied by the average selling price supplied by petitioner to arrive at sales in dollars for the test quarter. The inventory figures and purchase information were supplied in petitioner's sales tax return worksheets.

12. Audited taxable sales were determined to be $1,055,608.00 with sales tax due thereon of $89,726.00. Since tax reported on the returns was $88,477.00, a difference of $1,249.00, an

error rate of 1.41% (1249/88477) was established and applied to the tax reported for the entire audit period, $2,450,014.00, resulting in additional tax due of $34,545.00.

13. The Division utilized the information supplied by petitioner to establish net gallons sold per month and applied the sales tax paid per gallon ($0.10 for gasoline and $0.11 for diesel) to arrive at the correct prepaid tax on gallons sold during the test period.

The Division's examination of prepaid sales tax on petroleum products during the test quarter indicated that petitioner had reported a prepaid sales tax credit of $90,198.00. However, the Division's analysis indicated that petitioner was only entitled to $83,491.00, indicating that petitioner had overreported by 7.44%. The Division applied this percentage to the credit claimed by petitioner for the entire audit period, $1,846,826.00, to arrive at additional tax due for overreported prepaid tax credits of $137,404.00.

14. A review of the capital assets indicated that there were complete records for the entire audit period which revealed a total of $5,542.00 in untaxed assets, yielding additional tax due of $462.96. Reported convenience store sales, prepaid cigarette tax and expense purchases were analyzed and accepted as reported.

15. Petitioner's accountant, Mr. Schneiderman, explained that the erroneous prepaid tax credit taken by petitioner on its sales and use tax return for the test quarter was a result of a transposition error which resulted in an overreported prepaid tax credit of $6,707.00, and that his prepaid tax calculation without the error equaled the Division's prepaid tax computation, despite the fact that he and the Division used different methods of computation. The exact location of the transposition error was not disclosed nor was there a detailed description of the error itself. In fact, Mr. Schneiderman conceded that there had been "three or four periods" where

transposition errors had been made with resultant overreporting of prepaid tax. However, he never identified the specific periods.

16. Petitioner filed a New York State and Local Quarterly Sales and Use Tax Return for Part-Quarterly Filers, form ST-810, for the test period, March 1, 2002 through May 31, 2002 on or about June 19, 2002, prepared by Mr. Schneiderman. Form ST-810.10 is also required of vendors selling motor fuel and provides for a calculation of tax adjustments including the prepaid sales tax credit. Although the form ST-810 was submitted in evidence by the Division with no objection by petitioner, the form ST-810.10 was not attached as required and petitioner made no offer of the form of its own. Any error in the computation of the prepaid tax credit would have been apparent on the form ST-810.10, since it set forth taxable sales of motor fuel and diesel motor fuel by taxing jurisdiction which would have provided the basic information to calculate the prepaid tax credit.

17. Petitioner submitted into evidence purchase invoices from OK Petroleum for diesel and gasoline for each month in the audit period except the months of June and July 2002 for gas and the months of March and July 2002 for diesel fuel. Therefore, the record does not contain all the purchase invoices for the test period nor was it established whether the invoices represented all fuel purchases.

18. Mr. Schneiderman equated gallons purchased with gallons sold in reporting sales on petitioner's sales and use tax returns, noting that he did so under the assumption that the opening and closing inventories were almost identical or within one or two hundred gallons and, therefore, were insignificant over the course of the audit period. Each reporting period, petitioner sent him records of the gallons purchased and pump price information to calculate the sales tax to be reported.

19. Petitioner maintained summaries of each day's transactions at its stations, comprised of a computer generated document, cash drop summaries, convenience store register tapes, credit card sales and cigarette sales information. The summary was referred to as a shift report. One such report was issued per day for each station, with the exception of stations which remained open for 24 hours, for which two reports may have been generated. Shift reports set forth the following: the gallons sold for the day by grade and the dollar amount of the sales; it included credit card sales (but it was noted that most credit card sales for fuel went directly to OK Petroleum); cash drops in the safe; sales of cigarettes; and sales of convenience store items. The shift reports did not show receipts for cash sales. The cash drops listed in the shift reports did not delineate the sources of the cash, whether it was received for fuel sales or otherwise. Shift reports were not produced in response to the initial request for all books and records pertinent to petitioner's sales and use tax liability nor were a substantial number of them produced to the Division at any time prior to the issuance of the Notice of Determination to establish petitioner's correct sales tax liability.

20. Some shift reports were shown to and utilized by the Division to establish petitioner's average pump prices in effect during the test quarter. Since the reports did not record individual sales, only summaries of total sales, the Division did not consider them reliable books of entry or original source documentation for sales of gas and diesel fuel; rather, they were seen as an informal summary or daybook with no backup documentation. Although petitioner's controller, Mr. John Mussachia, believed the shift reports to be the best evidence of sales that petitioner maintained, petitioner itself did not utilize the shift reports to prepare its sales and use tax returns because the process was considered too time-consuming. Instead, Mr. Musacchia sent Mr. Schneiderman summary sheets that stated the total gallons purchased and pump prices, from

which sales and prepaid tax was computed. The gallons-purchased figure on the summary was reported by the station managers who noted each delivery during the month. The pump prices were taken from the shift reports. In addition, the summary sheets sent to Mr. Schneiderman for preparation of the tax returns contained beginning and ending inventory amounts which were ignored for purposes of filing the sales tax returns. The summary sheets, like the purchase invoices produced by petitioner, could not be tied into the general ledger.

21. The Division was made aware of the shift reports during the audit when the taxpayer produced some samples to establish the actual pump prices for gasoline and diesel fuel. However, at no time during the audit was a complete set of the shift reports produced as documentation for actual sales made by petitioner, despite the requests by the Division for all books and records pertaining to petitioner's sales and use tax liability.

22. The Division mailed to petitioner a Statement of Proposed Audit Change, dated January 5, 2006, which explained that additional sales and use taxes had been determined in accordance with Tax Law § 1138, based upon an audit of petitioner's available records. The statement asserted additional tax due of $172,411.96, interest of $110,777.99 and penalty of $50,618.98 for a total amount due of $333,808.82 for the period December 1, 1999 through November 30, 2004. Included in the mailing with the statement was a copy of the audit workpapers.

23. Petitioner disagreed with the audit result and a conference was held on January 13, 2006 to discuss the Division's conclusions. Mr. Schneiderman voiced a particular objection to the overreporting of prepaid gasoline tax. Subsequently, after performing a review of two years of returns, Mr. Schneiderman informed the Division that the test quarter was the only one he found with a significant error. The Division considered this observation and offered him the

opportunity to provide additional documentation for two additional quarters, those ended August 31, 2001 and August 31, 2002. However, upon learning it was the Division's intention to average the results of the differences found in those quarters with the results of the test quarter, Mr. Schneiderman declined to provide the documentation, on the belief that such a methodology would still produce a large tax liability than was unwarranted.

24. After learning that no further documentation would be provided, the Division issued to petitioner a Notice of Determination, dated March 20, 2006, which asserted additional sales and use taxes due for the period December 1, 1999 through November 30, 2004 in the sum of $172,411.96, plus penalty and interest for a total amount due of $338,684.37.

25. Petitioner filed a petition for a conference in the Bureau of Mediation and Conciliation Services (BCMS) that was held on July 20, 2006. Petitioner contested the audit results on the basis that it always had adequate books and records which would have permitted a detailed audit but were never reviewed. Therefore, resort to an estimated audit methodology was not justified.

26. The conferee requested that the Division meet with petitioner to review the complete books and records, and a meeting was scheduled and took place on September 7, 2006. The day prior to the meeting, both the conferee and the auditor contacted Mr. Schneiderman to confirm that the complete books and records would be available for review and were informed that all the records would be available. In fact, petitioner did not produce the records promised, including any sales documentation, original source or otherwise; complete purchase invoices; and complete shift reports. At the meeting, the Division used the records for the quarter ended August 31, 2004, a quarter with records available, and determined that the purchases reflected on the invoices provided exceeded purchases set forth on the general ledger by approximately $325,000.00. Since this result undermined reliance on the purchase figures used to estimate sales

by both the Division and petitioner, the Division decided not to rely on any of the documentation provided.

27. In an electronic mail message to the conferee, dated September 21, 2006, the team leader, Mr. Frank Grillo, stated that petitioner had only produced 49 percent of the records promised and that he was skeptical of the computer-generated purchase invoices produced because he feared they could be created and printed at will. Mr. Grillo explained that he and the auditors performed a test on the records for the quarter ended August 31, 2004, yielding the discovery of the discrepancy between the general ledger and purchase invoices. Since this test indicated an overstatement in prepaid sales tax and an understatement in sales tax remitted, Mr. Grillo believed the results of the test confirmed the findings of the audit and the Division's choice of a test period audit methodology in the absence of complete and adequate records.

28. Mr. Musacchia, petitioner's controller, conceded that petitioner and its supplier, OK Petroleum, were owned by the same person, and formal invoicing was not always deemed necessary for purchases between the two companies, which might have accounted for the discrepancy between the general ledger and the purchase invoices. Further, credit card payments for motor fuel purchases from OK Petroleum were settled directly into the bank account of OK Petroleum by the click of a button, a practice that was common for OK Petroleum but allegedly not disclosed to Mr. Schneiderman, causing further confusion when trying to reconstruct sales from purchase information. For these reasons, he informed the conferee that the Division's choice of a test period estimated audit methodology was justified in the absence of complete records.

29. On December 29, 2006, a conciliation order was issued sustaining the Notice of Determination.

SUMMARY OF THE PARTIES' POSITIONS

30. Petitioner contends that the Division did not follow proper audit procedure in requesting and reviewing its books and records and making a definitive determination that the records they reviewed were inadequate to perform a detailed audit. Instead, the Division immediately utilized a test period to estimate petitioner's sales and use tax liability for the audit period, a methodology that lacked a rational basis and resulted in an unreasonably inaccurate estimate of petitioner's tax liability.

31. Petitioner argues that the Division was aware during the audit that adequate books and records were available but chose not to request that they be produced for review. Further, petitioner maintains that the Division refused to review the records produced during the pendency of the conference proceedings before BCMS.

32. Petitioner contends that its shift reports and purchase invoices constituted records from which its tax liability for the audit period could have been calculated accurately, yet the Division refused to examine them.

33. Finally, petitioner believes that since the Notice of Deficiency was based upon a flawed and improper audit, no basis exists for the imposition of penalties.

34. The Division argues that petitioner has never produced adequate books and records from which it could have performed a detailed audit, even though requested to do on numerous occasions. In the absence of books and records sufficient to perform such an audit, the Division believes it was justified in resorting to an estimated audit methodology, which it argues was reasonable and reasonably calculated the taxes due.

35. The Division argues that petitioner bears the burden of proving that the assessment was erroneous and has not done so, citing a murky financial relationship between OK Petroleum

and petitioner and the concessions by petitioner's witnesses that the records were indeed insufficient to perform a detailed audit. The Division disagrees with petitioner's claim that the Division was duty-bound to use petitioner's partial records because that was all that was available and that was the intent of Tax Law § 1138, arguing that to do so would allow taxpayers to use partial records to conceal their true tax liability.

36. Finally, the Division maintains that petitioner has not demonstrated reasonable cause for the abatement of penalties, offering little, if any, evidence to establish that its failure to pay the correct tax due was due to reasonable cause and not wilful neglect. The Division adds that petitioner's failure to maintain and provide any sales records is, in itself, grounds for sustaining the penalties. Since the burden of proof rests with petitioner on the issue of entitlement to abatement of penalties, the Division argues that petitioner has not met its burden herein.

CONCLUSIONS OF LAW

A. Tax Law § 1105(a) imposes a sales tax on the receipts from every "retail sale" of tangible personal property except as otherwise provided in Article 28 of the Tax Law. A "retail sale" is "[a] sale of tangible personal property to any person for any purpose, other than . . . for resale as such . . ." (Tax Law § 1101[b][4][i]). Tax Law § 1138(a)(1) provides, in relevant part, that if a sales tax return was not filed, "or if a return when filed is incorrect or insufficient, the amount of tax due shall be determined [by the Division of Taxation] from such information as may be available. If necessary, the tax may be estimated on the basis of external indices . . . ." (Tax Law § 1138[a][1].) When acting pursuant to section 1138(a)(1), the Division is required to select a method reasonably calculated to reflect the tax due. The burden then rests upon the taxpayer to demonstrate that the method of audit or the amount of the assessment was erroneous (***see Matter of Your Own Choice, Inc.,*** Tax Appeals Tribunal, February 20, 2003).

B. The standard for reviewing a sales tax audit where external indices were employed was set forth in ***Matter of Your Own Choice, Inc***., as follows:

> To determine the adequacy of a taxpayer's records, the Division must first request ***(Matter of Christ Cella, Inc. v. State Tax Commn.***, [102 AD2d 352, 477 NYS2d 858]) and thoroughly examine (***Matter of King Crab Rest. v. Chu***, 134 AD2d 51, 522 NYS2d 978) 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, ***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 Giordano v. State Tax Commn.***, 145 AD2d 726, 535 NYS2d 255; ***Matter of Urban Liqs. v. State Tax Commn.***, 90 AD2d 576, 456 NYS2d 138; ***Matter of Meyer v. State Tax Commn.***, 61 AD2d 223, 402 NYS2d 74, ***lv denied*** 44 NY2d 645, 406 NYS2d 1025; ***see also***, ***Matter of Hennekens v. State Tax Commn.***, 114 AD2d 599, 494 NYS2d 208), that they are, in fact, so insufficient that it is "virtually impossible [for the Division of Taxation] to verify taxable sales receipts and conduct a complete audit" (***Matter of Chartair, Inc. v. State Tax Commn.***, 65 AD2d 44, 411 NYS2d 41, 43; ***Matter of Christ Cella, Inc. 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).
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> 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 Liqs. v. State Tax Commn.***, ***supra***). The estimate methodology utilized must be reasonably calculated to reflect taxes due (***Matter of W.T. Grant Co. v. Joseph***, 2 NY2d 196, 159 NYS2d 150, ***cert denied*** 355 US 869, 2 L Ed 2d 75), but exactness in the outcome of the audit method is not required (***Matter of Markowitz v. State Tax Commn.***, 54 AD2d 1023, 388 NYS2d 176, ***affd*** 44 NY2d 684, 405 NYS2d 454; ***Matter of Cinelli***, Tax Appeals Tribunal, September 14, 1989). The taxpayer bears the burden of proving with clear and convincing evidence that the assessment is erroneous (***Matter of Scarpulla v. State Tax Commn.***, 120 AD2d 842, 502 NYS2d 113) or that the audit methodology is unreasonable (***Matter of Surface Line Operators Fraternal Org. v. Tully***, 85 AD2d 858, 446 NYS2d 451; ***Matter of Cousins Serv. Station***, Tax Appeals Tribunal, August 11, 1988). In addition, "[c]onsiderable latitude is given an auditor's method of estimating sales under such circumstances as exist in [each] case" (***Matter of Grecian Sq. v. Tax Commn.***, 119 AD2d 948, 501 NYS2d 219, 221).

C. In the matter at hand, there is no doubt that the Division made at least two adequate, unequivocal and clear requests for all of petitioner’s records related to its sales tax liability for

the entire audit period. Petitioner did not heed the requests made by Ms. Buscemi and Mr. DeFilippis, choosing to characterize them as overly broad, pro forma or mere boilerplate. However, a taxpayer who dismisses such requests does so at his or her own peril. This was particularly true herein, where petitioner had no sales records at all and prepared its sales tax returns from summary sheets of purchases and average pump prices, even ignoring beginning and ending inventory figures. Essentially, petitioner was approximating its tax liability for sales tax reporting purposes while failing to keep records of sales.

Tax Law § 1135(a) provides that every person required to collect tax shall keep records of every sale, the amounts paid on those sales and the tax due thereon. The regulations promulgated thereunder at 20 NYCRR 533.2(b)(1) dictate that the sales records required by Tax Law § 1135(a) *must* contain the sales slip, invoice, receipt, contract, statement or other memorandum of sale (20 NYCRR 533.2[b][1][i]), cash register tapes and any other original sales documents (20 NYCRR 533.2[b][1][iii]). In addition, the regulations require that where no written document is given to the customer, the seller shall keep daily records of all cash and credit sales in a day book or similar book. (20 NYCRR 533.2[b][1][iii].) These provisions bear witness to the spirit and intention of Tax Law § 1135(a), which was to insure that the records required to be kept provide sufficient detail to independently determine the taxable status of each sale and the amount of tax due and collected thereon or be substantiated by an analysis of supporting records. (20 NYCRR 533.2[b][2].)

The record amply demonstrates that sales records for motor fuels[1] were not maintained as prescribed by Tax Law § 1135(a) and the regulations promulgated thereunder, and no other

[1] As mentioned in the facts, the focus of the audit was fuel sales which remain as the only contested part of the sales tax audit. Additional tax on fixed assets was not contested by petitioner and convenience store sales, prepaid cigarette tax and expense purchases were analyzed and accepted as reported.

source documentation of sales existed. From the first meeting at Mr. Schneiderman's office on November 27, 2002 and throughout the audit, petitioner failed to produce the records necessary to perform a detailed audit. Further, petitioner did not maintain sales records pertaining to its sales tax liability which disclosed in verifiable detail the basis for the accuracy of the entries reported on the sales tax returns. (***See*** TSB-M-81[9]S.)

At the initial meeting with the Division, only a small fraction of the records requested was produced and no records of sales. Petitioner produced federal income tax returns, sales and use tax returns and worksheets for the period March 2001 through August 2002, year end trial balances for 2001 and 2002 and purchases reflected on check disbursements. In an effort to explain the lack of records, Mr. Schneiderman told the auditor that those records would be too voluminous, if not impossible, to produce. Presumably, the Division was informed at this time that sales records were not maintained and did not exist, but was not told that the voluminous records to which he referred were the shift reports and purchase invoices. Mr. Schneiderman conceded all along that sales records were not maintained and never existed and that he had no records for the first seven months of the audit period, before he was employed by petitioner.

Upon review of petitioner's records that were made available and its method of preparing and filing its sales tax returns, it was evident that petitioner utilized an estimated methodology based upon summaries of monthly purchases of motor fuels and a calculated average pump price to determine its sales tax liability. With this limitation, the auditor began a series of tests on the information provided which ultimately led to the decision to test sales of fuel for the period March 1, 2002 through May 31, 2002. At this juncture, Ms. Buscemi left the Division's employ and Mr. Defilippis continued the audit. On June 9, 2005, he made a second complete request for books and records for the expanded audit period December 1, 1999 through November 30, 2004.

Additionally, several other requests for records were made during the pendency of the audit. Although some records were produced in response to the requests, they were not satisfactory evidence of the sales reported by petitioner because none was source documentation.

It is clear from the record that the Division reviewed the records presented by petitioner and correctly concluded that they were not adequate to do a complete audit since there were no source documents, i.e., sales invoices, complete purchase invoices or cash register tapes, submitted by petitioner (***see Matter of Vebol Edibles v. State of New York Tax Appeals Tribunal***, 162 AD2d 765, 557 NYS2d678, ***lv denied*** 77 NY2d803, 567 NYS643; ***Matter of Club Marakesh v. Tax Commn. Of State of New York***, 151 AD2d 908, 542 NYS2d 881, ***lv denied*** 74 NY2d 616, 550 NYS2d 276). Further, during the audit petitioner did not produce a complete general ledger, a complete set of shift reports for the purpose of establishing sales, or any evidence of cash sales of fuel. Neither the purchase invoices nor the summary sheets used by petitioner to complete its sales tax returns tied into the general ledger. Under these circumstances, it was not possible for the Division to verify taxable sales and receipts and conduct a complete audit.

D. Petitioner maintains that the shift reports it maintained constituted original source documentation of sales that were reviewed by the Division for pump prices but not requested for purposes of establishing sales. In fact, the shift reports are raw summaries of a day's operations which include gross numbers for sales of fuel in gallons and dollars, cash drop summaries, convenience store register tapes, credit card sales figures and cigarette sales. The information contained in the reports was not itself auditable because there was no source documentation underlying the data for most of the entries, i.e., there was no documentation which would allow one to trace a transaction from purchase of the commodity to the final sale transaction with the

customer, most notably for motor fuel sales. Further, there was no breakdown of cash sales for fuel and there was no accounting for the substantial number of credit card sales which were settled directly to OK Petroleum. Despite petitioner's claim that the shift reports were an accurate record of its sales, they were not original source documentation which identified individual sales, and even petitioner did not avail itself of them in preparing its own sales tax returns, instead choosing to use purchase records to create summaries for Mr. Schneiderman, who never questioned or investigated the underlying information he was provided. Further, since Mr. Schneiderman only used the purchases listed on the summaries given to him for preparation of the tax returns, choosing to ignore the opening and closing inventories, his entries on the returns were estimates without any source documentation behind them. Although he protested that he was not an auditor, it seems that a prudent tax return preparer would have asked if the information he was provided was supported by original source documentation.

In ***Matter of A & A Service Station, Inc.*** (Tax Appeals Tribunal, February 5, 2004), the Tribunal held that the Division's use of shift "sheets" to determine petitioner's true tax liability in an estimated audit methodology was reasonable. Unlike the instant matter, A & A voluntarily produced the sheets for the entire audit period for the purpose of establishing meter readings in dollars and gallons for each of petitioner's ten pumps and set forth fuel inventories. Like the instant matter, A & A ignored the information on the shift sheets and filed its sales tax returns based on motor fuel purchases and then multiplied by the average price per gallon for each grade of gas. The shift sheets indicated a large discrepancy in the number of gallons of gas stated on the paid invoices and A & A was held liable for the tax on the additional gallons. Here, the Division used the shift reports provided for the purpose of determining an accurate average pump price for calculating a sales figure to petitioner's advantage. Although petitioner was in a position to offer

all the reports for the purpose of establishing its sales and use tax liability or constructing a coherent presentation of sales data from which an accurate portrayal of its sales could be exposed, it chose not to. Its argument that it failed to produce them because it was never asked to do so is frivolous. The formal requests for records clearly requested all books and records pertaining to the sales and use tax liability for the audit period. If petitioner believed that the shift reports could establish its sales tax liability with accuracy, it would have offered them in response to the Division's requests.

However, from Mr. Schneiderman's testimony, it is apparent that this would not have agreed with what petitioner reported and was likely why petitioner did not produce the shift reports. Petitioner prepared its returns using summary purchase figures in gallons to which it applied an average pump price, not actual sales as reported in the shift reports. Opening and ending inventories were ignored. Thus, petitioner's methodology for preparing its returns would never agree with the sales recorded on the shift reports and would supply little support for the accuracy of the returns filed. However, as stated, the shift reports were not original source documentation and, if produced, would have been subject to scrutiny for their failings.

E. Having established that the records were so insufficient that it was virtually impossible to verify taxable sales by means of a complete audit (***Matter of Chartair, Inc. v. State Tax Commn.***), the Division was entitled to resort to an estimate of petitioner's sales, as long as the method was reasonably calculated to reflect the taxes due. (***Matter of Grant v. Joseph***, 2 NY2d 196, 159 NYS2d 150 [1957], ***cert denied*** 355 US 869 [1957].)

The Division chose to use a method which was very similar to the methodology petitioner used in preparing its returns, with the exception that the Division utilized the opening and ending inventories supplied by petitioner to Mr. Schneiderman, yielding a more accurate determination

of gallons sold. To this it applied the average pump prices, supplied by petitioner, less excise and sales tax for each grade of gas and diesel to arrive at a taxable sales figure. This methodology produced an error rate of only 1.41% for the tested quarter ended May 31, 2002. The difference may be explained by petitioner's practice of ignoring inventory in its calculation of gallons sold. Although petitioner speculated that the inventory will always be sold over time, and therefore need not be considered in calculating sales and sales tax liability, it does not lend itself to accuracy for any given quarter, and any deficiency caused by taking this risk remains with petitioner.

The single largest component of the deficiency was the credit for prepaid tax. Once again, the Division and petitioner used the same methodology: gallons sold multiplied by either $0.10 for gas or $0.11 for diesel. As with the audit methodology for sales, the Division determined an error rate for the overreporting of the prepaid tax credits for the tested quarter. However, the error rate for the prepaid tax credits was calculated to be 7.44%. Although Mr. Schneiderman claimed this was due to a transposition error, he never identified it. Additionally, the form ST-810.10, part of the sales tax return required to be filed by vendors of motor fuel and which includes the calculation of the prepaid sales tax credit, was omitted from the return for that test quarter which was submitted into evidence. This omission prevented the detection of the error in the computation of the credit since the ST-810.10 sets forth taxable sales of motor fuel and diesel motor fuel by taxing jurisdiction, providing the basic information to calculate the credit.

Mr. Schneiderman also conceded that he was aware of three or four other periods with errors but never identified them. Although Mr. Schneiderman insisted that the test quarter was one of only a few periods with errors, he refused to submit additional documentation for two other quarters when invited to do so by the Division, saying that the Division's intention to

average the differences found in the three quarters would result in an unacceptably large deficiency for petitioner, even though it would have underscored the error, if any, in the test period and bolstered his argument that an isolated error had caused the large overreporting of the prepaid sales tax credit.

The use of the test period, or quarter, based on petitioner's own documentation of gallons purchased as gallons sold was both consistent and fair with respect to prepaid tax credits, especially when considered in light of the results reached in testing for additional taxable sales and the fact that petitioner used a very similar, if less accurate, methodology. The Division, in estimating the corporation's tax liability, was required to select a method reasonably calculated to reflect the tax due (***see e.g. Matter of ADGN, Inc.***, Tax Appeals Tribunal, February 2, 1997). It is well established that exactness in the audit result is not required, for any imprecision that arises from the taxpayer's failure to maintain adequate books and records as required under the Tax Law is properly borne by the taxpayer (***see Matter of Chronos Enterprises***, Tax Appeals Tribunal, December 13, 2007). It is well established that the test period is an acceptable audit method (***see e.g. Matter of Continental Arms Corp. v. State Tax Commn.***, 72 NY2d 976, 534 NYS2d 362 [1988]).

Petitioner's argument that a transposition error was the sole cause of the large discrepancy is without merit since it offered nothing to prove where the mistake was made. Even the form ST-810.10 for the test quarter, which would have identified the mistake was not offered. Further, when afforded the opportunity to challenge the results of the test quarter, it declined on the basis that to do so would subject it to an inequitable assessment. Unfortunately, petitioner has offered no proof of the alleged mistake or that its credits claimed in other quarters were substantiated. In fact, Mr. Schneiderman further eroded confidence in his claim that the test

quarter was a mere outlier when he admitted he knew of mistakes made in reporting prepaid tax credits in other unidentified quarters in the audit period.

F. Petitioner had the burden of proof to show, by clear and convincing evidence, that the result of the audit was unreasonably inaccurate or that the amount of tax assessed was erroneous (***see Matter of Your Own Choice, Inc.,***). Petitioner failed to meet this burden as it offered no evidence to refute the audit results. Rather, petitioner offered a general, yet elaborate, complaint regarding the use of a test period audit method instead of an alternative methodology. As determined above, it was immediately apparent and conceded by petitioner that it maintained no sales records, leaving the Division no choice but to use an indirect audit methodology to ascertain if petitioner had accurately reported its taxes. Without original source documentation the Division utilized petitioner's own records to test its tax reporting on the basis of purchases and pump prices, the same information available to petitioner when it prepared its returns. It used the same information to determine the proper amount of prepaid tax credits, which was consistent with and derived from its test of motor fuel sales. The Division was under no obligation to utilize and test information that was not original source documentation, information not used by petitioner and, not least of which, was never produced for the entire audit period.

G. Petitioner's contention that the Division refused to examine its records at the September 7, 2006 meeting at Mr. Schneiderman's office even though all the records were available is unfounded and rendered moot by the conclusions stated above. The meeting was held as a courtesy and only granted upon Mr. Schneiderman's representation that all the records would be available for inspection at the appointed time. Petitioner did not produce any source documentation for its sales during the audit period and did not have all shift reports and purchase invoices either. The test performed that day on the quarter ended August 31, 2004 yielded a large

discrepancy between purchases per invoices and those recorded in the general ledger, which further supported the Division's decision to resort to an indirect audit methodology. Thus, the Division was afforded no reason to change its position or audit methodology on the basis of what was presented and informed the conferee of same. Evidently, the conferee agreed since a BCMS order was issued sustaining the statutory notice.

H. In order to abate penalties, a taxpayer must show that the failure to comply with the law was due to reasonable cause and not due to willful neglect (Tax Law § 1145[a][1][iii]). Here, petitioner has not established that its underreporting of sales resulted from anything other than its own failure to maintain accurate records of sales and, therefore, as there has been no showing of reasonable cause and the absence of willful neglect for its failure to pay the sales and income taxes, there is no basis for abating the penalties assessed. (***Matter of Rosemellia***, Tax Appeals Tribunal, March 12, 1992.)

I. The Petition of Straight Path Service Station, Inc. is denied and the Notice of Determination, dated March 20, 2006, is sustained.

DATED: Troy, New York
December 30, 2008

/s/ Joseph W. Pinto, Jr.
ADMINISTRATIVE LAW JUDGE