

STATE OF NEW YORK
STATE TAX COMMISSION

In the Matter of the Petitions
of
THOMAS J. SPINOSA AND ANTHONY DiPRIMA
for Revision of Determinations or for Refunds
of Sales and Use Taxes under Articles 28 and 29
of the Tax Law for the Period December 1, 1973
through February 28, 1977.

DECISION

Petitioners, Thomas J. Spinosa and Anthony DiPrima, 3289 East River Road, Rochester, New York 14623, filed petitions for revision of determinations or for refunds of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1973 through February 28, 1977 (File Nos. 21450, 21451 and 24868).

A formal hearing was commenced before Julius E. Braun, Hearing Officer, at the offices of the State Tax Commission, One Marine Midland Plaza, Rochester, New York, on December 7, 1982 at 9:15 A.M. and continued to conclusion before Daniel J. Ranalli, Hearing Officer, at the same offices, on May 31, 1984 at 10:00 A.M., with all briefs to be submitted by October 14, 1984. Petitioners appeared by Max T. Stoner, Esq. The Audit Division appeared by John P. Dugan, Esq. (Thomas Sacca, Esq., of counsel).

ISSUE

Whether the Audit Division used proper audit procedures to determine petitioners' sales tax liability.

FINDINGS OF FACT

1. On September 13, 1977, as the result of a field audit, the Audit Division issued a Notice of Determination and Demand for Payment of Sales and

Use Taxes Due against petitioners, Thomas J. Spinosa and Anthony DiPrima, in the amount of \$34,274.60, plus penalty and interest of \$16,223.77, for a total due of \$50,498.37 for the period December 1, 1973 through February 28, 1977. The notice represented the tax liability for petitioners' store located on East River Road in Rochester, New York. On the same date, the Audit Division issued a second notice against petitioners in the amount of \$22,187.35, plus penalty and interest of \$10,789.73, for a total due of \$32,977.08 for the period December 1, 1973 through February 28, 1977. Said notice represented the tax liability for petitioners' store located on Fairport Road, Fairport, New York. On the same date, the Audit Division issued a third notice against petitioners in the amount of \$26,229.52, plus penalty and interest of \$12,232.38, for a total due of \$38,461.90 for the period December 1, 1973 through February 28, 1977. Said notice represented the tax liability for petitioners' store located on Ridge Road West, Rochester, New York. Identical notices for each of the three stores were also issued to each petitioner individually.

2. On March 31, 1977, petitioners had executed consents extending the period of limitation for assessment of sales and use taxes for the period December 1, 1973 through May 31, 1974 to September 20, 1977 for each of the three stores audited.

3. Petitioners are partners operating retail grocery stores under various names in the Rochester area. In setting prices for the goods sold in their stores, petitioners would have the general manager of the stores periodically check prices in other grocery stores in the areas around each of petitioners' stores. The general manager would then discuss his findings with petitioners. Petitioners and the general manager would then determine the appropriate profit margin for each category of item sold. These percentages were written down and

distributed to each store manager who would set prices accordingly. Thus, each of the three stores had the same profit margin as set by petitioners.

4. Each of the three stores maintained cash register tapes and receipts and disbursements records on a weekly basis. All of the records were brought to the bookkeeper at the main office who would do the weekly postings. The bookkeeper took the records, including the cash register tapes which were attached to the weekly invoices, and brought them to petitioners' accountant's office. The accountant prepared the sales tax returns from these records. The cash register tapes from petitioners' stores did not specifically identify each item that was sold, but showed only the price and whether tax was charged.

5. The Audit Division did a separate audit of each store. The auditor noted that the records for each store were well kept. The audit procedure utilized in each store was essentially the same. The auditor examined merchandise purchases during the three-month test period and derived a taxable ratio. This ratio was applied to reported purchases to determine taxable item purchases. A markup of taxable items was determined using selling prices and invoice costs from February, 1977. This markup was applied to taxable item purchases to arrive at audited taxable sales. Reported taxable sales were subtracted from audited taxable sales and multiplied by the tax rate to arrive at additional tax due. The additional tax due for the River Road store was \$34,038.21. The additional tax due for the Fairport Road store was \$21,939.48. The additional tax due for the Ridge Road store was \$26,108.91.¹

6. Petitioners argue that they maintained complete records including cash register tapes with which a complete audit could have been conducted and that

¹ Additional tax was also found to be due on expense purchases and capital purchases; however, these were minimal amounts and were not raised as an issue.

it was not necessary for the auditor to utilize a test period and purchase markup method of audit.

Alternatively, petitioners argue that, even if resort to a purchase markup test was warranted, the markups as computed were inaccurate because during the month selected as a test period by the auditor, petitioners were in the process of raising their price structure as suggested by their accountants. Petitioners performed their own markup test utilizing the profit margin sheets issued to each store manager during the audit period. This test, which involved months in 1974 and 1975, indicated markups lower than the auditor's by four to 25 percent. Petitioners also maintained that they incurred three to four percent losses due to spoilage and pilferage and that no allowance for such losses was given by the auditor.

7. Based on petitioners' tests the additional tax due should have been computed as follows:

	<u>River Road Store</u>				
	<u>Markup</u>	X	<u>Percent of Purchases</u>	=	<u>Weighted Markup</u>
Beer	1.299		.513		.666
Soda	1.299		.205		.266
Cigarettes	1.316		.131		.172
Candy	1.33		.035		.047
Other	1.401		.116		.162
<u>Total</u>					<u>1.313</u>

Taxable Purchases	\$574,401.11
Weighted Markup	X 1.313
Taxable Sales	<u>754,188.66</u>
Less Pilferage	<u>- .03</u>
	731,563.00
Reported Sales	<u>-289,755.75</u>
Additional Sales	441,807.25
Tax Rate	X .07
Additional Tax Due	<u>\$ 30,926.51</u>

<u>Fairport Road Store</u>				
	Markup	X	Percent of <u>Purchases</u>	= <u>Weighted Markup</u>
Beer	1.299		.376	.488
Soda	1.299		.138	.179
Cigarettes	1.316		.344	.453
Candy	1.33		.087	.116
Other	1.401		.055	.077
<u>Total</u>				<u>1.313</u>

Taxable Purchases	\$415,533.16
Weighted Markup	X 1.313
Taxable Sales	<u>545,595.04</u>
Less Pilferage	<u>- .03</u>
	529,227.19
Reported Sales	<u>-276,635.95</u>
Additional Sales	252,591.24
Tax Rate	<u>.07</u>
Additional Tax Due	\$ 17,681.39

<u>Ridge Road Store</u>				
	Markup	X	Percent of <u>Purchases</u>	= <u>Weighted Markup</u>
Beer	1.299		.571	.742
Soda	1.299		.195	.253
Cigarettes	1.316		.122	.161
Candy	1.33		.061	.081
Other	1.401		.051	.071
<u>Total</u>				<u>1.308</u>

Taxable Purchases	\$444,053.89
Weighted Markup	X 1.308
Taxable Sales	<u>580,822.49</u>
Less Pilferage	<u>- .03</u>
	563,397.81
Reported Sales	<u>-234,481.29</u>
Additional Sales	328,916.52
Tax Rate	<u>X .07</u>
Additional Tax Due	\$ 23,024.16

8. The Audit Division argues that, since each item sold was not specifically identified on the cash register tapes, the auditor could not determine if sales tax was charged on all taxable items. An audit of the cash register tapes would not have revealed whether taxable items were improperly rung up as nontaxable or whether sales were made off the cash register. The Audit Division

maintains that such tapes were inadequate for verifying taxable sales or ascertaining the exact amount of tax due.

CONCLUSIONS OF LAW

A. That section 1138(a) of the Tax Law provides that:

"If a return when filed is incorrect or insufficient, the amount of tax due shall be determined by the tax commission from such information as may be available. If necessary, the tax may be estimated on the basis of external indices, such as stock on hand, purchases, rental paid, number of rooms, location, scale of rents or charges, comparable rents or charges, type of accommodations and service, number of employees or other factors."

B. That although petitioners maintained all the register tapes for the audit period, each item sold was not specifically identified on the tapes and as a result the auditor could not determine if sales tax was charged on all taxable items. An audit of the cash register tapes would not have revealed whether taxable items were improperly rung up as nontaxable or whether sales were made off the cash register. The audit procedures utilized, even when based on petitioners' own figures, disclosed a significant variance with taxable sales reported indicating that sales tax was not properly charged on all items subject to tax.

C. That petitioner has proven that the audit findings were erroneous to the extent indicated in Finding of Fact "7" and accordingly the additional tax due is as follows:

River Road Store	\$30,926.51
Fairport Road Store	\$17,681.39
Ridge Road Store	\$23,024.16

D. That the petitions of Thomas J. Spinosa and Anthony DiPrima are granted to the extent indicated in Conclusion of Law "C"; that the Audit Division is directed to modify the notices of determination and demand for

payment of sales and use taxes due issued September 13, 1977 accordingly; and that, except as so granted, the petitions are in all other respects denied.

DATED: Albany, New York

STATE TAX COMMISSION

FEB 15 1985

Rodrick Allen
PRESIDENT

Francis D. Kolmg
COMMISSIONER

Walter J. ...
COMMISSIONER