STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition of JAMES G. KENNEDY & CO., INC., JAMES G. KENNEDY and RAYMOND LiCALZI 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 March 1, 1975 through May 31, 1979.	DECISION

Petitioners, James G. Kennedy & Co., Inc., James G. Kennedy and Raymond LiCalzi, 215 East 38th Street, New York, New York 10016, 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 March 1, 1975 through May 31, 1979 (File No. 29408).

A formal hearing was held before Robert F. Mulligan, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on January 12, 1984 at 10:00 A.M., with final briefs submitted on May 4, 1984. Petitioners appeared by Cunningham & Lee, Esqs. (Gerard W. Cunningham, Esq., of counsel). The Audit Division appeared by John P. Dugan, Esq. (Thomas C. Sacca, Esq., of counsel).

ISSUES

I. Whether it was proper for the Audit Division to perform a test period audit where all books and records were available.

II. Whether a certain purchase from Distinctive Hardware was a representative purchase for purposes of the audit.

III. Whether petitioner James G. Kennedy & Co., Inc. is entitled to credit for sales taxes paid in March and April 1975 on charges for carting services.

IV. Whether penalties should be cancelled.

FINDINGS OF FACT

1. Petitioner James G. Kennedy & Co., Inc. is a general building contractor based in New York City.

2. On March 12, 1980, the Audit Division issued notices of determination and demand for payment of sales and use taxes due to petitioner James G. Kennedy & Co., Inc. for the following periods and respective amounts:

Periods	Total Tax Due	Penalty	Interest	Total
3/1/75-8/31/78	$35,382.32	$8,783.17	$13,966.79	$58,132.28
9/1/78-5/31/79	$ 7,748.87	$1,283.38	$ 946.84	$ 9,979.09

The notices stated that the taxes were determined to be due in accordance with said petitioner's records and were based on an audit thereof.

The notices were timely issued, as said petitioner had executed appropriate consents extending the period of limitation for assessment.

3. Also on March 12, 1980, the Audit Division issued similar notices of determination and demand for payment of sales and use taxes due to James G. Kennedy, president and Raymond LiCalzi, vice president of James G. Kennedy & Co., Inc. The notices were for the following periods and respective amounts:

Periods	Total Tax Due	Penalty	Interest	Total
3/1/75-8/31/78	$19,506.40	$4,839.15	$7,781.14	$32,126.69
9/1/78-5/31/79	$ 4,420.31	$ 748.89	$ 556.92	$ 5,726.12

These notices were issued on the basis that said petitioners were personally liable as officers of James G. Kennedy & Co., Inc. under sections 1131(1) and 1133(a) of the Tax Law. Mr. Kennedy and Mr. LiCalzi have not challenged the determination that they are personally liable for any tax owing by the corporation; accordingly, the term "petitioner" as used herein will refer solely to the corporation.

4. The assessments were protested by a letter dated March 27, 1980, which was received by the Department of Taxation and Finance on April 1, 1980. A perfected petition dated April 11, 1981 was received by the Tax Appeals Bureau on May 15, 1981.

5. A sales tax audit of petitioner was conducted by the Audit Division.

a) Books and records were found to be adequate. Petitioner's representative agreed to the use of test periods and found the periods selected to be fair.

b) Reported sales were found to be accurate.

c) The first two pages (approximately three weeks) of the billing ledgers for September, 1977 were tested. Originally, the auditor disallowed 5.5 percent of nontaxable sales. However, after an informal District Office conference held on November 19, 1979, disallowed nontaxable sales were reduced to .63 percent.

d) Subcontractor material purchases were tested for July, 1976 and 2.7 percent, or $14,039.00, were disallowed. At the District Office conference, petitioner contended that this amount included nontaxable debris removal and capital improvements, as well as a unique purchase of $4,749.00 from Distinctive Hardware. Petitioner claimed that the unique purchase was not representative and should not be projected over the audit period. Petitioner also claimed that it erroneously picked up the purchase on its books as a subcontractor purchase rather than as a material purchase. At the conference, petitioner substantiated $8,759.00 of the $14,039.00 which had been disallowed as being nontaxable capital improvements. Of the balance, $531.00 represented debris removal from capital improvement sites. Consequently, the Audit Division did not assess debris removal made prior

to September 1, 1976 (the effective date of 20 NYCRR 527.7, which provided that said removal charges were taxable), on the basis that petitioner had acted on an opinion of Counsel to the Department of Taxation and Finance which had stated that such charges were not taxable. (The regulation section was subsequently invalidated by the April, 1982 decision of the Appellate Division, Third Department, in Building Contractors Association, Inc. v. Tully, 87 A.D.2d 909.)

A detailed examination of all debris removal purchases made after September 1, 1976 was performed, resulting in additional taxable rubbish removal purchases of $18,458.00.

The purchase from Distinctive Hardware was found to be similar to purchases from Architectural Hardware, another of petitioner's suppliers, who also charged no tax, apparently because it was located in New Jersey. Said purchase was removed from the category "subcontractor purchases" and added to "material purchases".

As a result of the above, the tax due on subcontractor purchases was deleted.

(e) Material purchases were tested for July, 1976 and February, 1978 and $5,928.00, or 17 percent of the total for the two months, was disallowed. This percentage was applied to the period April, 1975 through February, 1978 resulting in the disallowance of $142,665.00. March, 1975 was examined separately because of unusually large material purchases resulting in a disallowance of $39,072.00. At the conference, petitioner contended that $2,848.00 of the $5,928.00 disallowed materials purchases for the test months represented $2,697.00 nontaxable debris removal, invoices upon which tax had been paid and a one-time item upon which tax of $151.00 was

not charged. As the result of the conference, debris removal prior to September 1, 1976 was not assessed (as per above) and the $151.00 was not projected over the audit period. The $4,749.00 purchase that had been erroneously posted to subcontractor purchases was added to the $3,079.00 materials purchases assessed resulting in total disallowed purchases of $7,828.00 for the test months, or 19.8 percent. When applied to the purchases for the period April 1, 1975 through May 31, 1979, this percentage resulted in a disallowance of $227,688.00.

(f) Sales tax accrued on taxable sales was compared to the sales tax paid on the returns filed by petitioner for the audit period. This resulted in additional sales tax due of $3,804.01. This was not reduced at the conference and, in fact, the comparison was updated to May 31, 1979 and additional tax increased to $3,902.59.

(g) The auditor examined fixed asset additions for the entire audit period and found that no additional tax was due.

(h) Tax collected and expense purchases were tested and no error found.

6. The materials purchase of $4,749.00 from Distinctive Hardware, a Connecticut supplier, was a unique purchase for a specific job at the specific direction of the architect. The auditor found that petitioner did not make any other purchases from Distinctive Hardware during the entire audit period.

7. At the informal conference held on November 19, 1979, petitioner claimed not only that allowance should be made for nontaxable debris removal, but also that it was entitled to a credit for any tax paid on its debris removal purchases.

8. The debris removal at issue was the carting away of construction or demolition debris from capital improvement projects.

9. On March 17, 1975, petitioner paid $6,012.00 in sales tax to B. V. Rubbish Removal Co., Inc. with respect to debris removal for the period March 3 to March 10, 1975 for the Telephone Building, 13th Street and 2nd Avenue, New York City. On April 7, 1975, petitioner paid the same hauler $3,680.60 in sales tax for debris removal for the same building for the period March 10 to March 21, 1975.

CONCLUSIONS OF LAW

A. That section 1138(a) of the Tax Law provides, inter alia, that if a sales and use tax return filed is incorrect or insufficient, the amount of tax due shall be determined by the State Tax Commission from such information as may be available. Although test period audits are generally used where books and records are inadequate, a taxpayer and the Audit Division may agree to use test periods even where books and records are adequate and available for examination. Such agreements are, in fact, commonplace in large audits involving voluminous records.

Here, petitioner's records were adequate and available for examination; however, petitioner's representative agreed to the use of the test periods and found the periods selected to be fair. Accordingly, petitioner's reliance on Chartair, Inc. v. State Tax Commission, 65 A.D.2d 44, is misplaced.

B. That the materials purchase from Distinctive Hardware was not a representative purchase and should not be applied to periods outside the test. The purchase was a unique purchase made at the specific request of the architect and the Audit Division found that petitioner made no other purchases from Distinctive Hardware at any other time during the audit period. Accordingly,

this purchase should not have been extrapolated to those portions of the audit period beyond the periods tested.

C. That section 1139(a) of the Tax Law provides, in pertinent part:

> "(a) In the manner provided in this section the tax commission shall refund or credit any tax, penalty or interest erroneously, illegally or unconstitutionally collected or paid if application therefor shall be filed with the tax commission (i) in the case of tax paid by the applicant to a person required to collect tax, within three years after the date when the tax was payable by such person to the tax commission as provided in section eleven hundred thirty-seven,...".

Assuming that the carting company filed quarterly sales and use tax returns (and nothing to the contrary has been shown), March, 1975 sales tax would have been remitted with a sales and use tax return for the period March 1, 1975 through May 31, 1975 which was required to have been filed on or before June 20, 1975. Accordingly, petitioner should have filed an application for credit or refund with the State Tax Commission by June 20, 1978. Although petitioner was not entitled to apply for a refund of tax after said date or apply for a credit on its sales tax returns due after said date, it is nevertheless entitled to offset the $9,692.60 in sales tax paid on debris removal in March and April 1975, plus interest, against the outstanding assessments.

D. That petitioner's failure to pay over the proper amount of tax was excusable and due to reasonable cause. Accordingly, the penalties imposed under section 1145(a) of the Tax Law are cancelled. Minimum interest only is to be added only to the tax found due herein.

E. That the petition of James G. Kennedy & Co., Inc., James G. Kennedy and Raymond LiCalzi is granted to the extent indicated in Conclusions of Law

"B", "C" and "D" and is in all other respects denied. The notices of determination and demand for payment of sales and use taxes due are to be reduced in accordance herewith.

DATED: Albany, New York

MAR 14 1985

STATE TAX COMMISSION

PRESIDENT

COMMISSIONER

COMMISSIONER