

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition  
of  
LUCILLE'S FOOD CENTER  
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, 1979  
through August 31, 1982.

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DECISION

Petitioner, Lucille's Food Center, 4619 South Salina Street, Syracuse, New York 13205, 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 December 1, 1979 through August 31, 1982 (File No. 42839).

A hearing was held before Arthur Bray, Hearing Officer, at the offices of the State Tax Commission, 333 East Washington Street, Syracuse, New York, on July 11, 1985 at 9:15 A.M., with all briefs and documents to be submitted by August 14, 1985. Petitioner appeared by Sugarman, Wallace, Manheim & Schoenwald (Donald L. Schoenwald, Esq., of counsel). The Audit Division appeared by John P. Dugan, Esq. (James Della Porta, Esq., of counsel).

ISSUE

Whether petitioner has sustained its burden of proof of establishing entitlement to an adjustment of an assessment of sales and use taxes on the ground that it suffered losses due to theft.

FINDINGS OF FACT

1. On March 18, 1983, on the basis of a field audit, the Audit Division issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due for the period December 1, 1979 through August 31, 1982 to Lucille's Food

Center ("Food Center") assessing sales and use tax due of \$8,655.40, plus penalty of \$1,775.00 and interest of \$1,886.35, for a total amount due of \$12,316.75.

2. The Food Center was a convenience grocery store which was owned and operated by Lucille Morris. The Food Center sold beer, soft drinks, cigarettes, candy and various food items. It was located in a low-income area on East Fayette Street in Syracuse, New York.

3. The Food Center had one entrance for customers. As one entered the store, the cash register and counter were located on the left. The beer cooler was located in the back of the store over thirty feet from the cash register. A person operating the cash register could generally observe the activity at the beer cooler. However, a portion of the view of the beer cooler was obstructed by a pillar.

4. In the course of the audit, the Audit Division requested to see petitioner's books and records. With the exception of the year 1981, the Audit Division was supplied with petitioner's records of sales and purchases. Information with respect to the year 1981, including the cash receipts book and check disbursements book, was not made available by either petitioner or petitioner's accountant. Moreover, petitioner's Federal and New York State income tax returns, though requested, were not provided.

5. Petitioner provided the Audit Division with those portions of her cash register tapes showing total sales by category for a day. The categories consisted of items such as beer or taxable groceries. The tapes disclosed the amount of sales tax collected on each category of sales. The portions of the tapes showing the items purchased and the selling price were not retained. Petitioner did not have a complete set of cash register tapes because of

periodic problems with the cash register. In addition, petitioner did not always use a tape with her cash register.

6. In the course of the audit, the Audit Division observed that the transaction number of ending sales for one day did not always coincide with the beginning sales for the next day. The Audit Division also observed that, for the year 1980, beer purchases of \$23,367.19 were recorded on petitioner's records, while beer sales were recorded at \$12,636.17.

7. The Audit Division concluded that a markup test was warranted because of the discrepancy between beer purchases and beer sales. The period of March 1, 1982 through May 31, 1982 was chosen as the period to test the markup on purchases since it was felt this would be the most reliable way to determine the business' markup. The markup test revealed that the markup on beer was 37.93 percent. The Audit Division also conducted a weighted markup test on taxable grocery items resulting in a markup of 29.43 percent. The foregoing markups were applied to the Food Center's purchases as disclosed by the books and to audited purchases where records were not available. These computations resulted in additional beer sales of \$70,120.10 and additional taxable merchandise sales of \$54,777.51 for total additional sales of \$124,897.61. The latter amount was reduced by a one percent inventory shrinkage factor to arrive at additional taxable sales of \$123,648.65 and additional tax due of \$8,655.40. The one percent inventory shrinkage factor was not intended to allow for theft losses. The reason why an adjustment for theft was not made was because petitioner did not submit documentary substantiation of thefts at the time of the audit.

8. It was petitioner's practice to record information from cash register tapes in ledger books. When the cash register did not have a tape, the cash register would still provide information on the day's sales. Peti-

tioner's accountant would prepare petitioner's tax returns on the basis of the information in the ledger book.

9. The Food Center suffered substantial losses from theft. The location of the beer cooler permitted individuals to conceal beer under their jackets and then leave without paying. In addition, it was difficult to watch individuals' activities at the beer cooler while the proprietor was serving customers at the cash register. During the period in issue, petitioner discovered that distributors of beer were not delivering all of the cases of beer which were contracted for. The Food Center also suffered losses from pilferage by its employees and from being burglarized. As a result of the foregoing, ten percent of the Food Centers' inventory was lost.

#### CONCLUSIONS OF LAW

A. That in determining the amount of a sales tax assessment, it is the duty of the Audit Division to select a method "'reasonably calculated to reflect the taxes due' (Matter of Grant Co. v. Joseph, 2 N.Y.2d 196, 206)." (Matter of Meyer v. State Tax Comm., 61 A.D.2d 223, 227 lv. to app. den. 44 N.Y.2d 645). When the Audit Division employs such a method, it becomes incumbent upon the petitioner to establish error (Matter of Meyer v. State Tax Comm., supra).

B. That section 1138(a) of the Tax Law provides, in part, that if a return required to be filed is incorrect or insufficient, the Tax Commission shall determine the amount of tax due on the basis of such information as may be available. This section further provides that, if necessary, the tax may be estimated on the basis of external indices.

C. That resort to the use of a test period to determine the amount of tax due must be based upon an insufficiency of record keeping which makes it

virtually impossible to determine such liability and perform a complete audit (Matter of Chartair, Inc. v. State Tax Commission, 65 A.D.2d 44). Petitioner did maintain some books and records which were available to the Audit Division. These records, however, were insufficient for verification of taxable sales, as the Audit Division could not determine from the tapes and records available whether tax had been charged on all taxable items or whether proper tax had been charged in each instance. Accordingly, the Audit Division's use of a markup audit to estimate the tax due from petitioner was reasonable under the circumstances (Matter of Licata v. Chu, 64 N.Y.2d 603).

D. That upon all of the facts and circumstances presented herein, including the ample evidence presented that petitioner has sustained substantial losses due to theft and delivery shortages, it is found that petitioner's total sales found on audit should be reduced by ten percent in addition to the allowance for inventory shrinkage described in Finding of Fact "7".

E. That in view of the substantial discrepancy between the sales found on audit, even after the adjustment made in Conclusion of Law "D", and the sales which were reported, petitioner has not presented a basis for the remission of penalty.

F. That the petition of Lucille's Food Center is granted to the extent indicated in Conclusion of Law "D" and the Audit Division is directed to modify the Notice of Determination and Demand for Payment of Sales and Use Taxes Due accordingly; the Notice is, in all other respects, sustained.

DATED: Albany, New York

FEB 18 1986

STATE TAX COMMISSION

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER