

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

ALBERT AND FRANCES OLSEN

for Redetermination of a Deficiency or for
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Years 1979, 1980 and
1981 and Unincorporated Business Tax under
Article 23 of the Tax Law for the Years 1979
and 1980.

DECISION

In the Matter of the Petition

of

ALBERT OLSEN D/B/A OLSEN'S SERVICE 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, 1980
through November 30, 1981.

Petitioners, Albert and Frances Olsen, RD 1, Box 141, Babcock Road,
Harpursville New York 13787, filed a petition for redetermination of a deficiency
or for refund of personal income tax under Article 22 of the Tax Law for the
years 1979, 1980 and 1981 and unincorporated business tax under Article 23 of
the Tax Law for the years 1979 and 1980 (File No. 43163).

Petitioner, Albert Olsen d/b/a Olsen's Service Center, RD 1, Box 141,
Babcock Road, Harpursville, New York 13787, 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, 1980 through November 30, 1981 (File No.
50780).

A hearing was held before Dennis M. Galliher, Hearing Officer, at the offices of the State Tax Commission, 164 Hawley Street, Binghamton, New York, on November 20, 1986 at 10:45 A.M., with all briefs to be submitted by January 30 1987. Petitioners appeared by Philip J. Devine, Esq. The Audit Division appeared by John P. Dugan, Esq. (Deborah J. Dwyer, Esq., of counsel).

ISSUES

I. Whether petitioners may properly make a claim for refund of sales and use taxes previously assessed upon audit, consented to and paid by petitioners and, if so, whether (and in what amount) petitioners are entitled to a refund.

II. Whether the Audit Division's assertion of an income tax deficiency based upon the results of the aforementioned sales tax audit was proper and, if so, whether petitioners have established any basis for reduction or abatement of such deficiency.

III. Whether petitioners have established any basis which warrants reduction or cancellation of any of the penalties imposed.

FINDINGS OF FACT

1. On June 17, 1982, the Audit Division issued to petitioner Albert Olsen d/b/a Olsen's Service Center a Notice of Determination and Demand for Payment of Sales and Use Taxes Due assessing additional sales tax due for the sales tax quarterly periods ended February 28, 1979 through November 30, 1981 in the aggregate amount of \$4,875.65 plus interest. A validated consent executed by Albert Olsen allowed assessment for the quarterly period ended February 28, 1979 to be made at any time on or before June 20, 1982.

2. On March 16, 1983, the Audit Division issued three notices of deficiency to petitioners Albert and Frances Olsen, husband and wife, asserting additional

personal income tax due for the years 1979, 1980 and 1981 and unincorporated business tax due for the years 1979 and 1980, in the aggregate amount of \$7,476.83, plus penalty and interest. Petitioners had timely filed New York State personal income tax resident returns, and unincorporated business tax returns pertaining to Olsen's Service Center, for each of the years in question. A Statement of Audit Changes issued previously to petitioners on January 26, 1983 indicated that the asserted income tax and unincorporated business tax deficiencies were based on the results of the sales tax audit of Olsen's Service Center.

3. Prior to 1973, Mr. and Mrs. Olsen resided in Long Island, New York where Mrs. Olsen worked as a therapy aide in a Long Island hospital and Mr. Olsen worked as a welder.

4. Petitioners moved to Harpursville, New York in 1973.

5. Upon moving to Harpursville, petitioners learned of a then-vacant Mobil service station located in McClure, New York. Petitioners rented this service station from Mobil Oil Corporation in the summer of 1973 and began operation of the business known as Olsen's Service Center. Petitioners sold gasoline and petroleum products and, in addition, performed auto repairs and services. Petitioners had no prior experience in the operation of a service station or any other business.

6. In October of 1981, after eight years of operation, petitioners closed Olsen's Service Center.

7. During January, February and March of 1982, the Audit Division conducted a sales tax audit of the petitioners' business. The auditor initially went to petitioners' place of business, noted that it was then closed, and concluded

the balance of the audit at petitioners' accountant's office and at petitioners' home.

8. At the commencement of the audit, the auditor requested of petitioners all books and records pertaining to the operation of Olsen's Service Center. In turn, petitioners supplied sales tax returns and worksheets, Federal and State income tax returns, depreciation schedules, purchase invoices and a purchase invoice summary, and daily sales summary sheets including gasoline pump readings. The auditor noted that petitioners neither supplied nor had **available cash register tapes, sales invoices, or sales slips pertaining to** parts sales and repair services. In turn, the auditor asserted that without these source documents to back up the dollar amounts on the daily sales summary sheets pertaining to parts and labor, the records were inadequate for purposes **of** establishing an audit trail and verifying such amounts. Accordingly, the auditor turned to test period and projection audit methods in the determination of petitioners' sales and use tax liabilities.

9. The sales and use tax assessment, **as** calculated by the auditor, is comprised **of** three parts, as follows:

- a.) The auditor determined and assessed an amount due of **\$934.28** on gasoline sales, based **on** correction **of** an error in petitioners' method of calculating sales tax due on gasoline sales. The auditor determined sales tax due **on** gasoline sales by taking total gallons sold from petitioners' summary sheets (pump readings), subtracting therefrom **8** cents of gasoline tax per gallon and dividing the resultant amount by **1.07** to arrive at gasoline sales. Thereafter, sales tax due was calculated and, when compared to the amount of tax shown as due per petitioners' returns, resulted **in** the aforementioned **\$934.28** deficiency. Inasmuch as petitioners provided daily pump readings, the auditor utilized petitioners' figures pertaining to gasoline sold. As further verification of the correctness of such gallonage reported the auditor cross-checked petitioners' gallonage against gallonage reported by petitioners' supplier Mobil Oil Corporation for **1980**.

Since the figures provided by both parties agreed, the auditor accepted petitioners' reported gallons of gasoline sold.

- b) The second component of the assessment consists of use tax in the amount of \$70.00 calculated as due on the purchase of a truck body and a gasoline station stove upon which sales tax was not paid.
- c.) The third, and by far largest component of the assessment, resulted from the auditor's calculation of tax due on the sale of tires, batteries and accessories ("TBA") and labor services associated therewith. More specifically, the auditor compared the taxpayers' cost for parts (per purchase invoices) with the manufacturer's suggested retail selling price of such parts. This comparison revealed a 61 percent (suggested) markup, to which the auditor added 100 percent of the cost of the part (as an estimate of petitioners' labor charges) to arrive at a total markup on auto parts (and installation) of 1.61. This markup, utilizing 100 percent of a part's cost as the labor component, is based on the auditor's experience in similar audits. In addition, sales and installation of tires and tubes was computed using a markup of 21 percent on the cost of tires and tubes with no labor component included. Finally, the sale of soda was marked up at the rate of 49 percent over cost based on the auditor's experience.

10. The auditor applied the above-mentioned markups to petitioners' actual parts purchases per purchase invoices to arrive at petitioners' revenues received (taxable sales) from parts and labor, and calculated the amount of tax due thereon. The auditor added this tax amount together with the amount of tax due from the corrected gasoline sales tax method (see Finding of Fact "9-a", supra) to arrive at audited sales tax due. Such figure, when compared to sales tax reported by petitioners, resulted in an error rate of 6.7 percent which was applied to the amount of sales tax reported per quarter to arrive at the sales tax deficiency assessed.

11. As noted, a Notice of Determination and Demand was issued on June 17, 1982, assessing tax due in accordance with the results of the sales and use tax audit. In turn, petitioners consented to and paid this assessment on or about

July 26, 1982, and filed no petition to contest such assessment within ninety days of its issuance.

12. **As** noted previously, petitioners also received thereafter three notices of deficiency pertaining to income tax and unincorporated business tax for the years 1979, 1980 and 1981, which asserted deficiencies are based on the results of the aforementioned sales tax audit.

13. The income tax and unincorporated business tax deficiencies represent the mathematical result of including the additional sales determined on audit per year, (plus sales tax due on the same), as additional income to petitioners for each year, as follows:

	1979	1980	1981
Additional Sales Per Audit	\$21,099.00	\$26,035.00	\$20,643.00
Sales Tax Due on Additional Sales	<u>1,477.00</u>	<u>1,822.00</u>	<u>1,445.00</u>
Total Deemed Additional Income	<u>\$22,576.00</u>	<u>\$27,857.00</u>	<u>\$22,088.00</u>

In addition, penalties were asserted pursuant to Tax Law §§ 685(b) [negligence] and (c) [failure to make estimated tax payments].

14. Petitioners timely protested the income and unincorporated business tax deficiencies. At the same time, petitioners filed a claim for refund **of** the sales and **use** taxes previously assessed, consented to and paid. Petitioners' claim for refund was denied by letter dated February 2, 1984. Petitioners thereafter filed a petition contesting denial **of** the refund claim.

15. Petitioners, from the commencement of the operation of Olsen's Service Center, did not use a cash register, but rather used a cash drawer. Petitioners maintained the noted daily summary sheets as a means **of** tracking receipts and expenditures. These sheets reflected, inter alia, daily pump readings, as well as summary dollar amounts for receipts on gasoline sales, parts, accessories,

labor, etc., summary dollar amounts for payouts (expenditures), and a reconciliation of cash amounts and resultant cash "**short** or over".

16. From the time of commencement of the business through 1978, petitioner Frances Olsen worked three days per week at the business, while petitioner Albert Olsen worked full time at the business. **Mr.** Olsen worked as a mechanic, while **Mrs.** Olsen performed all of the paperwork pertaining to the business, including preparing the daily sheets, pricing and marking the parts inventory, etc. Petitioners' sales tax returns were prepared by an accountant hired by petitioners, based upon the information contained on the daily summary sheets as submitted monthly to petitioners' accountant.

17. In October 1978, **Mrs.** Olsen went back to work for New York State as a therapy aide at the Binghamton Psychiatric Center. Thereafter, she ceased working three days per week at the business and only transcribed the daily summary sheets.

18. According to petitioners, the details of proper pricing for parts and services were more closely reviewed during the years when Mrs. Olsen handled the paperwork for the business. When she ceased actively working at the station in 1978 the inventory pricing, and updating thereof, all fell to **Mr.** Olsen. **Mr.** Olsen's method **of** recordkeeping entailed using scraps of paper to keep track **of** repair sales and parts sales. These scraps of paper were transcribed onto the daily cash sheets and then discarded. Sales slips were generally not issued on each sale during the audit period because, according to Mr. Olsen, he "didn't think it was necessary".

19. Petitioners note that McClure, New York is a rural farming area, and is financially depressed with a high rate of unemployment. The station **is** located at the crossroads of Route 41 and Interstate 17, in a sparsely-populated

area. In addition to being termed a "poor recordkeeper" and "one who did not deal with detail", Mr. Olsen often charged no labor on the services he rendered, and sold parts at the amount either that he paid for them (at cost) or at the manufacturer's suggested retail prices in effect at the time of purchase of the parts. In essence, petitioners assert that parts and labor prices as charged did not keep track with inflation, and that in many instances, there was no charge at all for labor. Thus, petitioner's maintain the markups utilized on audit were not an accurate representation of the markups they used and do not accurately reflect receipts recieved by petitioners.

20. Petitioners computed sales of gasoline, and hence their receipts therefrom, based on their daily pump readings. Petitioners assert that they did not account for the fact that many times customers would drive up to the pumps, pump a quantity of gas, then reset the pumps, pump another lesser amount and only pay for the lesser amount. Petitioners noted this happened because there was no inside pump reading display and that it was not possible at a self-service station to always be at the pumps to keep track of the amount of gas pumped. In addition, petitioners testified to three or four theft **losses**, including the theft of parts and, on one occasion, the theft of money. Petitioners reported only one **of** such break-ins to the police and their insurance carrier for fear of losing their insurance coverage due to repeated break-ins and theft losses.

21. Petitioners also allowed many of their customers to run "charge" accounts whereby gas was sold to the customer **on** an ongoing credit basis.¹

1 These accounts are distinguished from credit card sales and, **in** fact, represent petitioner's extension of courtesy credit to their regular local customers.

Payment was to be made when and as the customer was able. Many times, these charge accounts were not paid at all. Petitioners estimate their losses on such accounts to have been hundreds of dollars. However, all sales on such charge accounts were reported as sales on the day when made and, hence, as receipts subject to tax based on petitioners' method of calculating gasoline sales based on daily pump readings.

22. After closing the station in 1981, Mr. Olsen took a job with New York State as an equipment mechanic. Both Mr. and Mrs. Olsen continue to work for the State, he as a mechanic and she as a therapy aide. Petitioners both testified that they closed the station because they were unable to make money in its operation.

23. It is petitioners' position that given Mr. Olsen's poor recordkeeping, his failure in many instances to charge any cost for labor on his services and the failure to update parts prices to even match the manufacturer's suggested selling prices supports their assertion that the audit markups were inappropriately high for their station and casts serious doubt upon the result of the major component of the sales tax audit. Petitioners maintain that they did not receive the markup amounts as asserted by the auditor, that in fact they lost money in the operation of the station, and that they, towards the latter part of the station's operation, borrowed money (as testified to by petitioners' banker) for current operating expenses on an ongoing short-term basis. Finally, petitioners note that they both went to work in their current positions in order that they could-earn money to meet basic living expenses, which expenses were not being met through operation of the service station.

CONCLUSIONS OF LAW

A. That the sales and use tax assessment issued to petitioners was a determination of tax due issued pursuant to Tax Law § 1138(a). In order to protest such assessment, petitioner were required to have filed a petition within ninety days of the issuance of such assessment (Tax Law § 1138[a]). **In** turn, Tax Law § 1139(c) provides, **in** part, as follows:

"[a] person shall not be entitled to a refund or credit... of a tax, interest or penalty which has been determined to be due pursuant to the provisions of section eleven hundred thirty-eight where he has had a hearing or an opportunity for a hearing, as provided in said section, or has failed to avail himself of the remedies therein provided."

B. That petitioners consented to and paid the assessment **in** question approximately **six** weeks after its issuance, and did not protest the assessment, request a hearing or otherwise avail themselves **of** the remedies available under section 1138 within the requisite time period. Accordingly, such assessment became finally and irrevocably fixed at the amount assessed and there **is no** basis upon which to grant petitioners a refund (Tax Law § 1139[c]).


C. That with respect to the income tax results arising from the sales tax assessment, it **is** noted that **no** independent income tax audit calculations were performed. We note further that it **is** not inappropriate, *per se*, to use a purchase markup analysis as a means of reconstructing a taxpayer's income for income tax purposes (Matter of William T. Kelly, State Tax Commn., December 31, 1984). However, petitioners herein have produced sufficient evidence **on** the record at hearing to show that the sales tax audit result was not an accurate indication of additional income flowing to petitioners during the years **in** question. Accordingly, the asserted deficiencies **in** income and unincorporated business taxes are cancelled (See Matter of D'Angelo, State Tax Commn.. March 27,

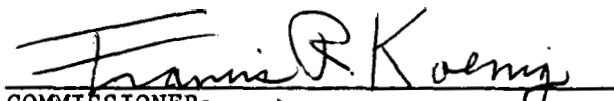
C. That the petition of Albert and Frances Olsen is hereby granted and the notices of deficiency issued on March 16, 1983 are cancelled. That the petition of Albert Olsen d/b/a Olsen's Service Center is hereby denied and the Audit Division's denial of petitioner's claim for refund of sales and use taxes paid is sustained.


DATED: Albany, New York

STATE TAX COMMISSION

APR 15 1987


PRESIDENT


COMMISSIONER


COMMISSIONER