

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition

of

PARKWAY AUTO SERVICE CENTER, 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 June 1, 1980
through August 31, 1983.

In the Matter of the Petition

of

PATRICIA DE MARIA

DECISION

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 June 1, 1980
through August 31, 1983.

In the Matter of the Petition

of

JOSEPH DE MARIA

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 June 1, 1980
through August 31, 1983.

Petitioner, Parkway Auto Service Center, Inc., 711 Tower Mews, Oakdale, New York 11769, 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 June 1, 1980 through August 31, 1983 (File No. 48046).

Petitioner, Patricia DeMaria, 711 Tower Mews, Oakdale, New York 11769, 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 June 1, 1980 through August 31, 1983 (File No. 50369).

Petitioner, Joseph DeMaria, 711 Tower Mews, Oakdale, New York 11769, 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 June 1, 1980 through August 31, 1983 (File No. 50370).

A consolidated hearing was held before Jean Corigliano, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on January 28, 1987 at 9:15 A.M., with additional information to be submitted by March 6, 1987. Petitioners appeared by Patricia DeMaria and Joseph DeMaria. The Audit Division appeared by John P. Dugan, **Esq.** (Michael B. Infantino, **Esq.**, of counsel).

ISSUES

I. Whether the Audit Division properly estimated petitioners' sales tax liability **on** the basis of external indices.

II. Whether petitioners are entitled to an abatement **of** penalty and interest above the minimum.

FINDINGS OF FACT

1. On August 23, 1983, the Audit Division issued to petitioner Parkway Auto Service Center, Inc. ("Parkway") a Notice of Determination and Demand for Payment **of** Sales and Use Taxes Due for the period June 1, 1980 through August 31, 1982 asserting total tax due in the amount of \$81,034.43 plus penalty and interest. On December 6, 1983, the Audit Division issued two notices to petitioners Joseph DeMaria and Patricia DeMaria, respectively, for the same period. Each notice asserted total tax due of \$81,034.43. In each case,

liability was predicated upon the respective petitioner's position as a responsible officer of Parkway.

2. On December 6, 1983, the Audit Division issued three notices of determination and demands for payment of sales and use taxes due for the period September 1, 1982 through August 31, 1983 in the amount of \$7,327.48 plus penalty and interest to Parkway, Joseph DeMaria and Patricia DeMaria. Again, Mr. and Mrs. DeMaria's liability was predicated upon their positions as responsible officers of Parkway.

3. Parkway operated a Mobil gasoline service station located off the Sunrise Highway in Islip Terrace, New York. It began doing business in January 1978 and continued until September 27, 1983.

4. The two sets of notices, covering different periods, resulted from an audit which proceeded in two stages. The first stage was a desk audit performed by the Central Office Audit Bureau ("COAB"), and the second stage was a field audit conducted by a district office auditor.

5. On June 27, 1983, COAB received from Parkway a completed Filling Station Questionnaire which provided information regarding its purchases and sales **for** the period December 1, 1981 through February 28, 1982. As requested, Parkway also provided copies **of** its 1980 and 1981 Federal corporation income tax returns.

6. COAB then made a comparison of gasoline purchases, as reported by Parkway, and gasoline purchases, as reported by Parkway's distributor, Mobil Oil Corporation ("Mobil"). To do **so**, COAB first adjusted Mobil's reported annual figures to obtain an average monthly figure. The comparison disclosed a discrepancy between Mobil's average monthly gasoline purchases for 1982 and Parkway's reported figures for the three month test period. In addition, there

was a discrepancy between the cost of goods sold as reported on Parkway's 1981 Federal Schedule C and its purchases of gasoline in 1981 as reported by Mobil. Finally, there was a discrepancy between Parkway's gross sales as reported on its sales tax returns and gross receipts as reported on its Federal income tax returns. Because of these discrepancies, COAB determined that Parkway's books and records were not sufficiently accurate to verify its reported taxable sales, and it proceeded to estimate sales taxes due on the basis of the information available to it.

7. COAB estimated additional taxes due, using a markup of purchases technique.

(a) COAB first determined a weighted average gasoline selling price to be applied to gasoline purchases.

(i) On its questionnaire, Parkway reported its selling prices on June 15, 1983 as follows: Self service: regular - 117.9; unleaded - 124.9; super unleaded - 139.9. Full service: regular - 129.9; unleaded 139.9; super unleaded - 149.9. The questionnaire also stated that Parkway had only self-service pumps and prices during the earlier three month test period for which COAB had requested purchase information.

(ii) COAB averaged the six selling prices reported by Parkway for this one day and compared this average to the statewide average selling price of gasoline for the quarter June 1, 1983 through August 31, 1983. The comparison showed that Parkway's prices were 3.4 percent higher than the statewide average for the same period. Consequently, for each of the nine quarters under consideration, COAB determined Parkway's average gasoline selling price by increasing the statewide average by 3.4 percent.

(b) The average selling prices, as determined above, were decreased by the excise and sales taxes included in the price, and the result was applied to gasoline purchases reported by Mobil. This resulted in audited taxable gasoline sales for each quarter.

(c) Based on its experience gained from other gasoline station audits, COAB estimated repair services and other sales at 20 percent of gasoline sales. Therefore, it increased Parkway's audited gasoline sales by 20 percent to obtain total audited taxable sales in each quarter.

(d) The appropriate sales tax rate was applied to audited taxable sales, yielding audited tax due for each quarter. Sales taxes paid by Parkway were subtracted from audited taxes due, resulting in additional tax due for the audit period of \$81,034.43.

8. After taxes were assessed against Parkway on the basis of COAB's audit, the second stage of the audit was conducted by a field auditor.

9. When the field audit began, Parkway already had ceased operations and had sold the assets it owned in connection with the station. The auditor requested from Parkway and received: a cash receipts journal, a check disbursements journal, purchase invoices and State and Federal tax returns. Sales invoices which were requested were not available because they had been transferred to the station's new owners to be used as a customer list.

10. During this second audit period, gasoline retailers were not directly responsible for reporting and paying over taxes collected on gasoline sales. Therefore, the audit was limited to receipts from sales other than gasoline.

11. Because sales invoices were not available and purchase figures from Parkway's cash disbursements journal and Federal income tax return were not reconcilable, the auditor deemed Parkway's books and records inadequate to

verify its reported taxable sales. Consequently, she attempted to verify sales through an analysis and markup of purchases.

(a) Using Parkway's cash disbursements journal, the auditor categorized its purchases for the period December 1, 1982 through February 28, 1983 as follows:

Gasoline	92.2919%
Oil	1.1464%
Tires	.7356%
Batteries	.2900%
Parts & Acc.	3.6462%
Sublet	,1734
Other	.8909%
Snackshop	.8256%

(b) The above percentages were applied to Parkway's total purchases for the audit period (\$1,443,759.23), as shown in its cash disbursements journal, to determine a dollar amount of purchases in each category. Parts purchases of \$52,642.35 estimated in this manner were increased by \$3,769.12 to reflect cash purchases as shown in Parkway's cash receipts journal. This resulted in audited parts purchases of \$56,411.47. Based on her professional experience, the auditor applied the following markups to purchases in each category: oil - 100%; tires and batteries - 40%; parts and accessories - 200%; snackshop - 66-2/3%. The markups included labor charges on repair services. This yielded audited taxable sales of \$242,932.93. The auditor added to this sublet sales (sales resulting from referrals from other service stations) of \$2,503.48 to calculate total audited taxable sales of \$245,436.51. Parkway's

1 "Sublet" and "other" purchases were not purchases of goods for resale. Apparently, they represent other expenses and were included in this analysis in order to account for 100 percent of the items in the cash disbursements journal.

reported taxable sales were subtracted from this to determine additional taxable sales of \$101,051.51, with a tax due on that amount of \$8,450.93 for the period September 1, 1982 through August 31, 1983.

12. From the fall of 1980 through the end of the audit period being considered, extensive construction work was taking place on Sunrise Highway, where Parkway's station was located, During the construction period, parts of the road were torn up making travel difficult. As a result, fewer drivers used the road, and business along the highway decreased. The decline in Parkway's business is reflected in the purchase figures obtained from Mobil which show 1,320,536 gallons of gasoline purchased in 1980, 929,641 gallons purchased in 1981 and 880,686 gallons purchased in 1982.

13. Petitioners challenge the audit results primarily on the basis that the decline in business occasioned by the highway construction forced Parkway to operate at a very slim profit margin and, at times, at a **loss**; thus, they argue, the markups used by the Audit Division did not reflect Parkway's markups and resulted in an overstatement of taxable sales.

14. In support of their position, petitioners offered a substantial amount of documentation.

(a) A complete set of original delivery tickets (or Mobil customer invoices) were offered for eleven months of 1982. These invoices tended to substantiate Mobil's record of purchases as reported to the Audit Division, but they also explained the discrepancy between the Filling Station Questionnaire submitted by Parkway and Mobil's figures. Parkway reported the exact number of gallons purchased in December 1981 and January and February of 1982. The Audit Division compared these figures to an average monthly figure calculated from Parkway's calendar year purchases for 1982. Since Parkway's monthly purchases

fluctuated, especially from the winter to the summer months, the actual purchase figures for the winter months were much lower than the average monthly figure.

(b) Newspaper advertisements taken from a local Pennysaver substantiate petitioners' claim that Parkway was operating at a low profit margin. For instance, State inspections were performed for no charge; there was no charge for towing customers to the station for repairs or services; and there were no labor charges for mounting and balancing tires purchased at the station. However, because no detailed sales or purchase invoices were submitted into evidence, it is not possible to use these advertisements to calculate actual markups.

(c) Because Parkway's sales were decreasing, Mobil assigned it a sales representative who negotiated gasoline purchase deductions and rent decreases for Parkway in an effort to help it continue operating through the period of construction. The sales representative periodically completed a form entitled "Service Station Operating Analysis" where, among other things, he recorded actual gasoline selling prices; receipts from the sale of tires, batteries, accessories, oil and repair services; and total expenses. He also calculated a markup for each month on gasoline sales and on all sales other than gasoline. These documents show an average markup on purchases other than gasoline of 57.222 percent. These records also establish that Parkway operated at a net loss throughout 1982.

(d) Various documents were submitted to show actual gasoline prices charged during the audit period. These include the documents described above as well as daily shift sheets and photographs. These documents established that during the period June 1, 1980 through August 31, 1982, actual selling prices equaled 93 percent of the statewide average selling price.

(e) The documents submitted by petitioner establish that for the period June 1, 1980 through August 31, 1982, Parkway's taxable sales other than gasoline amounted to 12 percent of its gross gasoline sales.

15. Petitioners base their request for abatement of penalties and interest above the minimum upon the ground that unwarranted legal actions taken by the Department of Taxation and Finance ("the Department") prevented them from paying certain taxes owed to the Federal government and caused interest and penalty to accrue unnecessarily. **When** Parkway ceased doing business in September 1983, **its** assets were sold to a third party for \$33,467.44. The proceeds from this sale were placed in an interest-bearing escrow account. Both the Federal and State governments had outstanding claims against Parkway based on its tax liabilities. The Department filed a notice with petitioners' escrow agent which effectively prevented any disbursements from the escrow funds. The Department and the Internal Revenue Service ("IRS") each asserted the priority of its own tax lien. On December 6, 1984, petitioners brought an interpleader suit in Federal court in order to clarify **the** status of the claims against the escrow fund. The Department eventually conceded the priority of the IRS lien, but it opposed a request for attorney's fees made by petitioners' representatives. On January 24, 1986, the United States District Court of the Eastern District of New York issued an order granting the request for attorney's fees. It **is** petitioners' position that the Department frustrated the timely and proper disbursement of the escrow fund resulting in increased legal expenses, interest and penalty charges.

CONCLUSIONS OF LAW

A. That under section 1135 of the Tax Law, every person required to collect tax **is** also required to keep records of every sale and of all the

amounts paid, charged or due on that sale and of the tax payable on each sale. Where such records are not made available upon the request of the Audit Division, or where, upon examination, the records are deemed insufficient to verify taxable sales, the Audit Division is authorized by Tax Law § 1138(a)(1) to determine the tax due from such information as may be available; where necessary, the tax may be estimated on the basis of external indices (En-Toto Beautiques of Manhasset v. State Tax Commission, 81 AD2d 680). That in light of the fact that information provided on the Filling Station Questionnaire and sales tax returns could not be reconciled with information reported on Federal returns, COAB was warranted in concluding that Parkway's books and records were inadequate to verify reported taxable sales. Likewise, the district office auditor's inability to reconcile records presented to her on audit justified a resort to external indices to determine Parkway's sales tax liability.

B. That in the absence of verifiable records, the Audit Division may select any audit methodology reasonably calculated to reflect sales taxes due, and the taxpayer must then show that the method of audit or amount of tax assessed was erroneous (Carmine Restaurant, Inc. v. State Tax Commission, 99 AD2d 581). Although the markup of purchases employed by the Audit Division was an acceptable methodology, petitioners have presented documentary evidence establishing that they are entitled to the following adjustments: (1) in each quarter of the period June 1, 1980 through August 31, 1982, the average selling price of a gallon of gasoline will be reduced to 93 percent of the statewide average selling price; (2) for the same period, Parkway's repair services and other taxable sales will be calculated at 12 percent of its gasoline sales; and (3) for the period September 1, 1982 through August 31, 1983, the markup

percentage to be applied to all purchases other than gasoline will be reduced to 57.222 percent.

C. That penalties and interest exceeding the statutory minimum may be waived by the State Tax Commission if the petitioner establishes that the failure **to** comply with the Tax Law was due to reasonable cause and not to willful neglect (Tax Law § 1145(a)). Grounds for reasonable cause are set forth in 20 NYCRR 536.5(b)(1) and may include the following:

"(1) death or serious illness of the taxpayer, a responsible officer or employee of the taxpayer, or his unavoidable absence from his usual place of business;

(2) destruction of the taxpayer's place **of** business or business records by fire or other casualty;

(3) timely prepared returns misplaced by the taxpayer or a responsible employee of the taxpayer and discovered after the due date;

(4) inability to obtain and assemble essential information required for the preparation of a complete return despite reasonable efforts;

(5) pending petition to Tax Commission **or** formal hearing proceedings involving a question or issue affecting the computation of tax for the year, quarter, month or other period of delinquency; or

(6) any other cause for delinquency which appears to a person or ordinary prudence and intelligence as a reasonable cause for delay in filing a return and which clearly indicates an absence of gross negligence or willful intent to disobey the taxing statutes. Past performance will be taken into account. Ignorance of the law, however, will not be considered reasonable cause."

D. That circumstances described by petitioners occurred after the tax liabilities were assessed (see Finding of Fact "15") and, therefore, they could not constitute reasonable cause for failure to accurately report and pay over taxes when due. The interpleader suit brought by petitioners did not involve a question or issue affecting the computation of tax. It was regrettable that interest and penalty charges accrued while that suit was pending; however, the


Department's determination to pursue its **own** legal remedies as provided for by law do not provide a basis for abating penalties, regardless **of** the outcome **of** the litigation.

E. That the petitions **of** Parkway Auto Service Center, Inc., Patricia DeMaria and Joseph DeMaria are granted to the extent indicated **in** Conclusion **of** Law "B"; that the notices of determination and demands for payment of sales and use taxes due, issued on August 23, 1983 and December 6, 1983, shall be modified accordingly; and that, in all other respects, the petitions are denied.

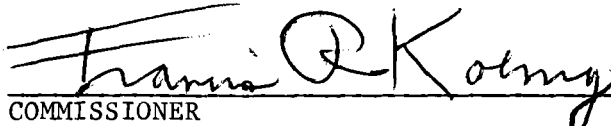
DATED: Albany, New York

STATE TAX COMMISSION


JUN 18 1987



PRESIDENT



COMMISSIONER



COMMISSIONER