

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
	:	
of	:	
	:	
ADASSA MEAT CORP. and	:	DECISION
ABDEL MUSTAFA and AHMED MUSTAFA, as Officers	:	
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 February 28, 1983.	:	

Petitioners, Adassa Meat Corp. and Abdel Mustafa and Ahmed Mustafa, as officers, 905 Franklin Avenue, Brooklyn, New York 11225, 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 February 28, 1983 (File Nos. 49487 and 49488).

A hearing was commenced before Doris E. Steinhardt, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on December 12, 1984 at 1:15 P.M. and continued to conclusion on April 1, 1985 at 1:15 P.M., with all briefs to be submitted by June 3, 1985. Petitioners appeared by Melvin L. Greenwald, Esq. The Audit Division appeared by John P. Dugan, Esq. (Irwin Levy, Esq., of counsel).

Petitioners' representative subsequently instituted an action in the Supreme Court, Kings County, to vacate a warrant of the State Tax Commission against Mohammed A. Mustafa. This action was discontinued by agreement of petitioners' representative and the Attorney General of the State of New York, and the hearing before the Tax Commission reopened to consider the identity of the corporate shareholders and officers. Accordingly, the hearing was reopened and held on July 8, 1985 at 1:15 P.M., with all briefs to be submitted by

August 26, 1985. Petitioners again appeared by Melvin L. Greenwald, Esq. The Audit Division appeared by John P. Dugan, Esq. (Patricia L. Brumbaugh, Esq., of counsel).

ISSUES

I. Whether a default should be issued against the Audit Division for its failure to file an answering pleading within the time period prescribed by the Rules of Practice and Procedure.

II. Whether the Notice and Demand for Payment of Sales and Use Taxes Due issued against Mohammed Ahmed Mustafa should be amended and reissued against Ahmed Mustafa.

III. Whether the Audit Division properly relied upon external indexes, in particular purchase information from a supplier and the results of a prior audit, to verify the sales and use tax returns filed by Adassa Meat Corp.

IV. Whether the failure of Adassa Meat Corp. to timely remit the proper amount of sales tax was due to reasonable cause and not to willful neglect.

FINDINGS OF FACT

1. On June 20, 1983, the Audit Division issued to petitioner Adassa Meat Corp. ("Adassa") a Notice of Determination and Demand for Payment of Sales and Use Taxes Due, assessing sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1979 through February 28, 1983 in the principal amount of \$321,212.26, plus interest and a delinquency penalty pursuant to section 1145(a)(1)(i). On June 20, 1983, the Audit Division issued to petitioner Abdel Mustafa under the name "Joe Mustafa" a Notice and Demand for Payment of Sales and Use Taxes Due, assessing sales tax for the period December 1, 1979 through February 28, 1983 in the amount of \$321,212.26, plus interest and penalties. On June 20, 1983, the Audit Division issued to Mohammed Abdel Mustafa

a Notice and Demand for Payment of Sales and Use Taxes Due, assessing tax, interest and penalty against him for the same taxable period and in an identical amount. Each Notice and Demand stated, in pertinent part:

"You are personally liable as officer of Adassa Meat Corp. under Sections 1131(1) and 1133 of the Tax Law for the...taxes determined to be due in accordance with Section 1138(a) of the Tax Law."¹

2. At the hearing convened on April 1, 1985, counsel to the Audit Division conceded that petitioners Adassa Meat Corp., Abdel Mustafa and Ahmed Mustafa all filed petitions in a timely fashion.

3. Adassa, a New York corporation organized in 1973, operates a supermarket in Brooklyn, New York. Its main supplier is Key Food Stores Cooperative, Inc. ("Key Food"). The sole shareholders and officers are Abdel (also known as Joe) Mustafa and his brother, Ahmed Mahmoud Mustafa. Mohammed (also known as Mike) Ahmed Mustafa is the son of Ahmed Mustafa. Mohammed performed general duties at the supermarket, including the supervision of personnel, on a part-time basis prior to June, 1981 and on a full-time basis thereafter.

4. In November, 1982, the Audit Division commenced an examination of Adassa's records and operations. Adassa was informed of the audit by letter and was requested to assemble all necessary documents, including ledgers, journals, bank statements, purchase invoices and cash register tapes; however, Adassa made available to the auditor only a limited number of documents: bank statements, the federal corporation income tax return for 1980 and several dozen purchase invoices. Adassa's sales as reported in its 1980 federal return

1 Insofar as the notices and demands were in compliance with section 1138(a) and the corporate officers raised no objection to the issuance of notices and demands rather than notices of determination and demands, each of the documents issued will be considered a Notice of Determination and Demand for Payment of Sales and Use Taxes Due.

exceeded sales as reflected in its bank deposits by the amount of \$101,185.00; purchases per the return exceeded purchases per bank records by \$78,854.00. The auditor discovered that during some months, Adassa's records indicated no purchases whatsoever. He therefore contacted Adassa's principal supplier, Key Food, to obtain Adassa's total purchases during one year falling within the audit period. In general, Key Food furnishes approximately 75 percent of the products sold in a Key Food supermarket. According to Key Food's records, Adassa's purchases during the eleven-month period December 1, 1981 through October 31, 1982 totalled \$1,868,733.00, as compared with purchases of \$203,115.00 shown in Adassa's records; this discrepancy represents a margin of error of 920 percent. (It must be noted that the assessments and the audit report on which they are predicated did not take into account bread, beer, soda, housewares and other products sold by Adassa but purchased from suppliers other than Key Food.) The auditor applied the 920 percent margin of error to Adassa's purchases throughout the audit period to arrive at adjusted purchases of \$7,627,608.00.

During the course of an earlier audit, which covered the period December 1, 1973 through November 30, 1977, an auditor had calculated that 37 percent of Adassa's purchases were taxable upon sale and that the overall markup over cost was 41 percent.² Based on Audit Division office experience and also the previous examination conducted of Adassa, the auditor employed a taxable ratio of 40 percent and a markup of 40 percent. These computations resulted in the assessment amount of \$321,212.26: tax due of \$345,785.75, less tax reported and paid of \$24,573.49.

2 The assessment resulting from the previous audit was reduced at a conference and as adjusted, satisfied by the corporation and/or the officers.

5. At the conclusion of the audit, assessments were issued, as above-stated, to Adassa, Joe Mustafa and Mohammed Mustafa. Believing that the Audit Division intended to assess the corporation and the corporate officers, petitioners' representative filed petitions on behalf of Adassa, Abdel (Joe) Mustafa and Ahmed Mustafa. After expiration of the ninety-day period provided by section 1138(a) for filing a protest, the Audit Division issued a warrant against Mohammed for the tax, plus accrued interest and penalties. This warrant remains in force, and petitioners ask the Tax Commission to vacate the warrant and to reissue the assessment against Mohammed in the name of Ahmed. It is unclear from the record and the briefs filed whether the Audit Division consents to petitioners' request. Further, Abdel and Ahmed do not contest their liability as persons required to collect tax on behalf of Adassa.

6. During the pendency of this proceeding, representatives of the Audit Division and of petitioners met to discuss the audit results and to attempt to resolve the matter without the necessity for a hearing. At this conference, petitioners presented two statements of account issued to Adassa by Key Food on June 14, 1984 and June 21, 1984, and two Key Food purchase invoices, one dated June 11, 1984 and consisting of fifty-five pages, the other dated June 18, 1984 and consisting of eleven (nonconsecutive) pages. Relying on this information to estimate Adassa's weekly purchases from Key Food, its taxable ratio of purchases and its markup, the Audit Division recomputed the sales tax, as shown below.

Average weekly purchases from Key Food	\$ 36,548
Average weekly cash purchases (estimated)	1,500
Average weekly purchases	\$ 38,048
Weeks in audit period	156
Purchases during audit period	\$5,935,488
Pilferage allowance 2½%	(148,387)
Net purchases	\$5,787,101
Taxable ratio 16.56%	16.56
Taxable purchases	\$ 958,344
Markup 22.22%	212,944
Taxable sales	\$1,171,288
Less: reported taxable sales	(279,785)
Additional taxable sales	\$ 891,503

Additional taxable sales \$891,503
Reported taxable sales \$279,785 = 318.64 margin of error

The Division then multiplied Adassa's reported taxable sales for each quarterly period under review by the recalculated margin of error and applied the appropriate tax rate to arrive at sales tax due of \$72,434.17. On October 10, 1984, the Audit Division prepared a Consent to Fixing of Tax Not Previously Determined and Assessed, indicating a principal amount of tax due of \$72,434.17, and delivered the Consent to Adassa's representatives with the understanding that full payment would be made shortly thereafter. Adassa refused to execute the Consent, alleging that the recomputation contained "categorical and mathematical errors." The corporation's independent accountants prepared and submitted to the Audit Division for its consideration their own proposal for settlement. The principal features of the accountants' proposal were: average weekly purchases from Key Food in the amount of \$34,766.00; the reduction of such figure by \$348.00, the one percent commission charged Adassa by Key Food; a taxable ratio of 14.6 percent; a pilferage allowance of 4 percent; and an allowance for "nonredeemable and double coupons" in the amount of \$131,040.00.

Average weekly purchases from Key Food	\$ 34,766
Less: commission of 1%	(348)
Cash purchases (estimated)	200
Average weekly purchases	\$ 34,618
Pilferage allowance 4%	(1,385)
Net weekly purchases	\$ 33,233
Taxable ratio 14.6%	14.6
Taxable weekly purchases	\$ 4,852
Weeks in audit period	156
Taxable purchases	\$756,915
Markup 22.22%	168,187
Total sales	\$925,102
Allowance for coupons	(131,040)
Taxable sales	\$794,062
Less: reported taxable sales	(279,785)
Additional taxable sales	\$514,277
Sales tax	\$ 41,785

The Audit Division rejected Adassa's counter-proposal. Petitioners resubmitted the proposal at the hearing held herein but failed to substantiate any of the aforementioned figures, with the exception of the commission payable to Key Food.

7. Petitioners seek waiver of the delinquency penalties assessed on the ground that the corporation always employed an accountant to attend to its books and accounts and prepare and file all required tax returns.

CONCLUSIONS OF LAW

A. That a default decision against the Audit Division for its failure to answer the petition within the time limitations set forth in the regulations (20 NYCRR 601.6[a][1]) is not warranted. The relevant provision of the Rules of Practice and Procedure is not mandatory, but directory only. (Matter of Santoro v. State Tax Comm., Albany Co. Special Term, January 4, 1979.)

B. That petitioner Abdel Mustafa and petitioner Ahmed Mustafa concede that as the sole officers and shareholders of Adassa, they were and are persons required to collect tax on the corporation's behalf; further, the Audit Division did not express opposition to petitioners' request that the assessment against

Mohammed Mustafa be reissued against Ahmed (Finding of Fact "5"). Accordingly, petitioners' request is granted, and the assessment issued on June 20, 1983 to Mohammed is amended to properly reflect Ahmed as corporate officeholder.

C. That the records Adassa furnished to the Audit Division for examination (bank statements, one federal corporation income tax return and some purchase invoices) were clearly inadequate to serve as verification of the corporation's taxable sales, and the Division thus appropriately employed external indexes for such purpose. The only question, then, is whether the audit procedure was reasonably calculated to reflect the taxes due. The Audit Division computed Adassa's purchases during the audit period by the application of a margin of error, such margin resulting from a comparison of purchases per Adassa's records and per Key Food's records covering the period December 1, 1981 through October 31, 1982. This method for arriving at purchases was acceptable, and petitioners did not satisfactorily establish that any error was made. The assessments should be recalculated, however, using a taxable ratio of 16.56 percent and a markup of 22.22 percent, which percentages were determined by reference to statements of account and invoices maintained by Adassa's principal supplier.³ The taxable ratio and markup underlying the original assessments were estimates, based on Audit Division experience and a prior audit of Adassa, and less accurately reflected the corporation's operations. A one percent reduction to purchases is also permitted, to take cognizance of the commissions paid by Adassa to Key Food.

3 Generally, an offer to compromise is inadmissible in evidence, but the Audit Division raised no objection to the introduction of the revised calculation (Finding of Fact "6"). Furthermore, the Key Food statements of account and invoices were themselves admissible evidence.

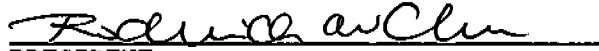
D. That petitioners did not establish that Adassa's failure to pay the correct amount of tax in a timely manner was due to reasonable cause and not to willful neglect. (See 20 NYCRR 536.1[b].) They did engage the services of a certified public accountant, but this factor is insufficient to counterbalance the deficiencies in their record keeping and the magnitude of their underreporting.


E. That the petition of Adassa Meat Corp. and Abdel Mustafa and Ahmed Mustafa, as officers, is granted to the extent indicated in Conclusions of Law "B" and "C"; the assessments issued on June 20, 1983 are to be modified accordingly; and except as so modified, the assessments are in all other respects sustained.

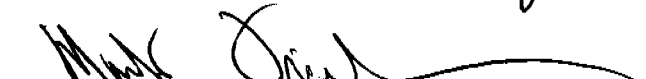
DATED: Albany, New York

STATE TAX COMMISSION

OCT 22 1985


PRESIDENT


COMMISSIONER


COMMISSIONER