

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition

of

FRANKLIN BEACON SPECIALTIES CORP.

DETERMINATION

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, 1979  
through February 21, 1983.

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Petitioner, Franklin Beacon Specialties Corp., 60 Crosby Street, New York, New York 10012, 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, 1979 through February 21, 1983 (File No. 55081).

On August 5, 1986, petitioner waived its right to a hearing in the Division of Tax Appeals and agreed to submit the case for determination based on the Division of Taxation file, with additional documents and briefs to be submitted by May 8, 1987. After due consideration, Daniel J. Ranalli, Administrative Law Judge, renders the following determination.

#### ISSUES

I. Whether petitioner has substantiated that certain of its sales were nontaxable because they were sales for resale.

11. Whether penalties and interest above the minimum should be abated.

#### FINDINGS OF FACT

1. On July 20, 1984, the Audit Division issued to petitioner, Franklin Beacon Specialties Corp., two notices of determination and demands for payment of sales and use taxes due under Articles 28 and 29 of the Tax Law: the first was for the period March 1, 1979 through August 31, 1982 and assessed sales and

use taxes of \$28,988.80 plus penalty and interest; the second was for the period September 1, 1982 through February 28, 1983 and assessed sales and use taxes of \$4,794.90 plus penalty and interest.

2. Petitioner, by its president, executed a series of six consents extending the period of limitation for the assessment of sales and use taxes under Articles 28 and 29 of the Tax Law for the period March 1, 1979 through March 31, 1981 to September 20, 1984.

3. Petitioner was engaged in the business of selling hardware, plumbing and restaurant supplies, primarily at wholesale. Petitioner also made retail sales of these goods. Generally, these were cash sales made at petitioner's place of business.

4. On audit, the auditor reconciled petitioner's general ledger to its Federal tax returns for the audit period and analyzed expense purchases for the months of June, July and August 1981. No discrepancies were found. As a result, the auditor deemed petitioner's books and records adequate to warrant their use in a detailed audit for the entire period. Upon being so advised, petitioner agreed to a representative test period audit.

5. For the audit period, petitioner reported gross sales of \$4,247,131.00 and taxable sales of \$114,877.00. The purpose of the audit was to determine whether substantiating documentation existed to support the claim of nontaxable sales. June of 1981 was selected as the test period.

(a) Petitioner's records showed nontaxable sales for the test period of \$101,215.76. The auditor examined the invoices of each sale and disallowed nontaxable status for each one not supported by a resale certificate deemed valid by the auditor. Many of the disallowed sales consisted of sales to out-of-state vendors who took possession of the merchandise at petitioner's

place of business. The auditor disallowed claimed nontaxable sales of \$10,217.21.

(b) A margin of error of 10.094 percent was calculated by dividing disallowed nontaxable sales by nontaxable sales as shown on petitioner's books. This percentage was applied to petitioner's reported nontaxable sales for the audit period to obtain total additional taxable sales of \$417,112.00 with a tax due on that amount of \$33,783.70.

6. Petitioner submitted a great many resale certificates and letters written by its customers to substantiate the \$10,217.21 in disallowed sales. Some of the New York State resale certificates were submitted by out-of-state vendors and bear resale identification numbers from other states. Some were New Jersey resale certificates which were completed in compliance with the statutes and regulations of New Jersey. One group of letters was from out-of-state vendors. Each one was typed on company letterhead, signed by a company owner or employee and stated, "This is to verify that the above named company came into New York to pick up merchandise which was used for Resale purposes." A second group consisted of a form letter sent by petitioner's president to a group of vendors and stated in part, "We would like confirmation from you that during the period March 1, 1979 through February 28, 1983 your purchases from us were for resale. If such was the case please acknowledge below and return this letter". These letters were signed and returned to petitioner.

7. Each individual sale disallowed by the Audit Division can be associated with a resale certificate or letter submitted by petitioner. The resale certificates represent \$6,897.38 of the disallowed sales, and the letters represent the remainder of the disallowed sales. In some cases,

petitioner submitted both a letter and a resale certificate for the same vendor.

8. It is the Audit Division's position that only nine of the resale certificates are adequate to substantiate petitioner's claims of nontaxability. It deems the others to be invalid certificates on one or more of the following grounds: (1) the purchaser identification numbers were not listed with the Audit Division; (2) the certificate is dated before or after the audit period; or (3) New Jersey resale certificates are invalid in New York State.

9. Petitioner requested abatement of the penalties asserted on the ground that the taxpayer's understatement of tax was unintentional and insubstantial, considering the size of its operations, the volume of its sales and the generally sound nature of its accounting system. As a result of the audit, petitioner now requires out-of-state customers to furnish an out-of-state resale permit.

#### CONCLUSIONS OF LAW

A. That Tax Law § 1132(c) provides, in pertinent part, that all receipts from the sale of tangible personal property shall be presumed to be subject to tax until the contrary is established, and the burden of proving that any receipt is not taxable shall be upon the person required to collect the tax, unless

"(1) a vendor shall have taken from the purchaser a certificate in such form as the tax commission may prescribe...to the effect that the property or service was purchased for resale'".

B. That vendors who accept in good faith properly completed resale certificates cannot "be held personally liable for sales taxes they failed to collect in reliance on certificates later found to have been improvidently issued" (Matter of Saf-Tee Plumbing Corp v. Tully, 77 AD2d 1, 4). Although

some of the resale certificates at issue were not in strict compliance with the provisions of section 1132(c) of the Tax Law and the regulations of the State Tax Commission promulgated under the authority of that statute, they appeared proper on their face, and they contained sufficient information to enable the petitioner to sustain its burden of proof to show that each sale made to a customer executing such a certificate was a sale for resale (~~see~~ Matter of Steelcase, Inc., State Tax Commission, July 3, 1986). Accordingly, petitioner has established that \$6,897.38 of the \$10,217.20 in disallowed sales for the test period were, in fact, sales for resale. Therefore, the margin of error to be applied to reported nontaxable sales for the audit period is reduced to 3.28 percent and the Audit Division is directed to recalculate petitioner's tax liability accordingly.

C. That the presumption of taxability may be overcome by sufficient evidence, and properly completed resale certificates are not the sole form of proof acceptable (Matter of Ruemil Contract Interiors, Inc., State Tax Commission, September 9, 1983). However, the letters from petitioner's out-of-state customers are not credible evidence of nontaxable sales. The legislature provided a specific statutory provision to insulate from sales tax liability vendors who obtain resale certificates from their customers (Tax Law § 1132[c]; Matter of Saf-Tee Plumbing v. Tully, 77 AD2d 1, supra). Having failed to obtain such certificates from these customers, petitioner bears the burden of showing that each purchase made by each of these customers during the test period was a purchase for resale. The simple assertion by these customers that all of their purchases were for resale is not sufficient to enable petitioner to carry its burden of proof.

D. That Tax Law § 1145(a) provides that any person failing to file a return or to pay over any tax as required by Article 28 of the Tax Law shall be subject to a penalty; however, the Tax Commission may remit all or part of such penalty, where the petitioner establishes that such failure or delay was due to reasonable cause and not to willful neglect.

E. That 20 NYCRR 536.5(b) provides that a "taxpayer's previous compliance record may be taken into account" in determining whether reasonable cause exists for waiving penalties. The regulation provides two examples of a situation in which a taxpayer's compliance record might be taken into account in determining whether penalties should be waived. The examples establish that reasonable cause may be found where the taxpayer has shown that it "made reasonable efforts to account for its sales tax liabilities, that the understatement of the tax was unintentional, ... that the [taxpayer] had...substantially complied with the law" (20 NYCRR 536.5[b][6][Example 1], and "[t]he understatement of the tax due was not...substantial taking into account the size of the operation, volume of sales and an otherwise sound accounting system" (20 NYCRR 536.5[b][6][Example 2])).


F. That petitioner has established by affirmative evidence that penalties and interest above the minimum should be waived. The Audit Division determined that petitioner's overall accounting system was sound and adequate for the purpose of verifying gross sales. Petitioner's sales journal and sales invoices were kept in good condition and allowed the auditor to identify each individual sale claimed by petitioner to be nontaxable. Petitioner produced resale certificates to substantiate the majority of its nontaxable sales. The remaining unsubstantiated sales to out-of-state vendors amounted to less than three percent of its total receipts for the test period. Since the audit,

petitioner has changed its accounting system to identify out-of-state customers and to require them to furnish an out-of-state resale permit or pay the sales tax due.

G. That the petition of Franklin Beacon Specialties Corp. is granted to the extent indicated in Conclusions of Law "B" and "F"; that the notices of determination and demands for payment of sales and use taxes due issued on June 20, 1984 shall be modified accordingly; and that, in all other respects, the petition is denied.

DATED: Albany, New York

SEP 11 1987

  
ADMINISTRATIVE LAW JUDGE