

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
GRB Chemists, Inc. : AFFIDAVIT OF MAILING
for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Sales & Use Tax :
under Article 28 & 29 of the Tax Law for the :
Period 6/1/75-2/28/79. :

State of New York }
County of Albany } ss.:

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 9th day of August, 1984, he served the within notice of Decision by certified mail upon GRB Chemists, Inc., the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

GRB Chemists, Inc.
446 Central Ave.
Cedarhurst, NY 11516

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
9th day of August, 1984.



Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
GRB Chemists, Inc. : AFFIDAVIT OF MAILING
for Redetermination of a Deficiency or Revision :
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under Article 28 & 29 of the Tax Law for the :
Period 6/1/75-2/28/79. :

State of New York }
County of Albany } ss.:

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 9th day of August, 1984, he served the within notice of Decision by certified mail upon Irwin Siegel, the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Irwin Siegel
Agins, Dolgin & Siegel
342 Madison Ave.
New York, NY 10173

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this
9th day of August, 1984.

David Parchuck

William R. Handman
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

August 9, 1984

GRB Chemists, Inc.
446 Central Ave.
Cedarhurst, NY 11516

Gentlemen:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1138 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Irwin Siegel
Agins, Dolgin & Siegel
342 Madison Ave.
New York, NY 10173
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
	:	
of	:	
	:	
GRB CHEMISTS, INC.	:	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, 1975	:	
through February 28, 1979.	:	

Petitioner, GRB Chemists, Inc., 446 Central Avenue, Cedarhurst, New York 11516, 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, 1975 through February 28, 1979 (File No. 28536).

A formal hearing was held before Daniel J. Ranalli, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on July 14, 1983 at 9:15 A.M., with all briefs to be submitted by November 7, 1983. Petitioner appeared by Irwin Siegel, Esq. The Audit Division appeared by John P. Dugan, Esq. (Michael Gitter, Esq., of counsel).

ISSUES

I. Whether the Audit Division properly determined petitioner's additional sales tax due.

II. Whether penalties and interest in excess of the statutory minimum should be waived.

FINDINGS OF FACT

1. On November 27, 1979, as the result of a field audit, the Audit Division issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due against petitioner, GRB Chemists, Inc., in the amount of \$58,590.59,

plus penalty of \$13,929.94 and interest of \$18,208.25, for a total due of \$90,728.78 for the period June 1, 1975 through November 30, 1978. On the same date, the Audit Division issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due against petitioner in the amount of \$4,239.99, plus penalty of \$551.19 and interest of \$348.95, for a total due of \$5,140.13 for the period December 1, 1978 through February 28, 1979.

2. On August 5, 1979, petitioner, by its secretary-treasurer, executed a second consent which extended the period of limitation for assessment of sales and use taxes due for the period June 1, 1975 through February 28, 1979 to December 20, 1979.

3. Petitioner operates a drug store under the name Robert's Pharmacy in Cedarhurst, New York. The front half of the pharmacy is used to sell over-the-counter drugs, cosmetics, perfumes, ice cream, candy and sundries. The rear half of the store is devoted to the preparation and sale of prescription drugs. The pharmacy is located on the main commercial street of Cedarhurst and there are several other drug stores nearby operating in competition with petitioner.

4. Petitioner maintained no cash register tapes or other original source documents of cash sales, but did maintain sales slips on its in-house credit accounts. Such credit sales constituted 47.9 percent of total sales according to a test of various months during the audit period performed by petitioner. In order to determine the amount of sales tax due for each quarter, petitioner's accountant estimated the percentage of taxable sales and applied it to gross sales per books. Petitioner's accountant generally used a taxable sales percentage of between 26 and 28 percent. The accountant had been told by the prior owners that that was the method they used and he continued to do it in the same manner.

5. On audit, the auditor found that, due to lack of internal accounting controls, gross sales per petitioner's books could not be verified; moreover, gross sales per petitioner's books were higher than gross sales per Federal income tax returns. Therefore, he found it necessary to resort to a markup test of taxable purchases. The auditor listed total purchases from each of petitioner's suppliers for one complete fiscal year. He then examined one month's invoices from each supplier to determine the percentage of taxable purchases from each vendor. Each percentage was applied to the total purchases from the respective supplier to find taxable purchases per supplier. The auditor then totalled the taxable purchases and divided the total by total purchases to arrive at a taxable ratio. The auditor computed a taxable ratio of 63.13 percent for the period prior to September 1, 1976 and 61.95 percent for the period after September 1, 1976.

6. The auditor then did a markup test using current invoices and current shelf prices for a day. The test included items on sale if the auditor had a current invoice available for such items. By this method, the auditor computed an average markup of 47.84 percent for the period prior to September 1, 1976 and an average markup of 48.09 percent for the period after September 1, 1976. The auditor allowed a 2 percent reduction of the computed markups for employee discounts, preferred customer discounts, special sales and cosmetic promotion sales, resulting in markups of 45.84 and 46.09 percent respectively. The auditor then applied the computed markup percentages to the taxable purchases computed to arrive at taxable sales. He then divided additional taxable sales by reported taxable sales to obtain a percentage of error of additional taxable sales of 120.05 percent. The auditor reduced taxable sales by 2.5 percent to allow for pilferage.

7. Petitioner's explanation for the discrepancy between gross sales per books and gross sales per Federal income tax returns was that sales per books included sales tax collected and bad checks given by customers. At the end of the year, petitioner's accountant subtracted the sales tax paid and customer checks which had been returned by the bank without payment. The final figure was the figure petitioner supposedly reported on its Federal income tax return. However, an examination of petitioner's reconciliation of bad checks and sales tax included in its sales per books showed such amounts to be \$5,332.00 in 1976, \$5,000.00 in 1977, and \$20,886.00 in 1978. The actual amounts of sales tax which were remitted during the audit period averaged \$12,800.00 per year. Thus, there remains a large unexplained discrepancy between gross sales per books and gross sales per federal returns. Petitioner maintained that its gross sales of \$2,604,915.00 reported on its Federal return approximated the gross sales as determined by the auditor. The auditor determined total taxable sales to be \$1,588,000.00 and taxable percentage of purchases of 62.5 percent. Petitioner argues that such determinations result in gross sales per audit of \$2,540,798.00, which was approximately \$60,000.00 less than petitioner reported on its Federal income tax return. Petitioner's argument assumes that the taxable percentage of purchases was the same as the taxable percentage of sales; however, no markups were computed on exempt purchases to determine exempt sales. Thus, gross sales were not established by a purchase markup audit.

8. Petitioner also argued that the auditor should have given weight to its in-house charge sales records which were complete for the audit period and which represented 47.9 percent of sales. Petitioner tested its charge sales for the entire month of October, 1977 and determined a percentage of taxable sales of 41.1 percent. Petitioner maintains that the latter figure is more

accurate than the 63.13 percent and 61.95 percent determined by the auditor. However, the numbered charge sales slips which were admitted into evidence had numerous missing numbers so that it is impossible to determine whether such sales were the total charge sales for the month tested by petitioner.

9. Petitioner's primary supplier was Drug Guild Distributors, Inc. ("Drug Guild"). Drug Guild purchases accounted for 42 percent of petitioner's total purchases for the audit period. On audit, the auditor tested Drug Guild purchases for two two week periods and arrived at a taxable percentage of 35.66 percent. Petitioner tested a different two week period and determined a taxable percentage of 20.5 percent with respect to Drug Guild purchases. Petitioner argued that its figure was more accurate than the auditor's because petitioner's figure would reduce the overall taxable percentage of petitioner's purchases to an amount closer to the figures for comparable drug stores as listed in the Lilly Digest, an annual pharmaceutical publication of Eli Lilly and Company which contains a survey of pharmacists across the country. The Drug Guild taxable purchases as determined by the auditor totalled \$74,000.00. According to petitioner's test, the Drug Guild taxable purchases were \$41,482.00.

10. Petitioner also maintained that in computing the markup percentages, the auditor did not sufficiently take account of petitioner's loss leaders, which were items sold at or below cost in order to compete with other pharmacies in the area. Petitioner did its own markup test on loss leaders purchased from Drug Guild and incorporated the result into the audit markup test for Drug Guild purchases. The result was a 9.6 percent markup on Drug Guild purchases as opposed to the 33.2 percent determined by the auditor. Petitioner's test, however, indicated that nearly one half of Drug Guild purchases were sold as loss leaders. There was no evidence presented supporting such a proposition.

11. Petitioner gave a 10 percent discount to certain customers on purchases of cosmetics and perfumes. Petitioner alleged that all of its cash customers received such a discount and, therefore, 50 percent of its sales involved the 10 percent discount. Petitioner maintained that the auditor should have made allowance for the discount. However, there was no documentation of the discount and no other evidence, other than the testimony of one customer, that one half of petitioner's customers consistently received a 10 percent discount.

12. Petitioner further argued that the 2.5 percent allowance for pilferage was insufficient due to the location of the store and its lack of security. When asked for a more accurate figure for pilferage, however, petitioner's secretary-treasurer was unable to determine a different figure.

13. The auditor determined that petitioner filed seven of fifteen returns late during the audit period and concluded that "taxable sales were grossly underreported" and recommended imposition of a penalty and maximum interest. Petitioner argued that it acted in good faith and did not understate its taxable sales. The testimony of petitioner's accountant, however, indicated that he prepared the returns in a timely fashion but that petitioner's officers would, for undisclosed reasons, leave the returns lying on the desk and not mail them in on time. Petitioner further argued that it did not understate the tax because it relied on percentages from its charge sales slips. However, petitioner's accountant testified that he used a taxable percentage of 26 to 28 percent and petitioner's own analysis of taxable charge sales revealed a taxable percentage of 41.1 percent, thus indicating that petitioner underreported by at least 14 percent.

CONCLUSIONS OF LAW

A. That section 1135 of the Tax Law, in effect during the period in issue, requires every person required to collect sales tax to keep records of every sale and of the tax payable thereon. "Such records shall include a true copy of each sales slip, invoice, receipt, statement or memorandum...". Section 1138(a) provides that if a sales tax return "is not filed, or if a return when filed is incorrect or insufficient, the amount of tax due shall be determined by the tax commission from such information as may be available. If necessary, the tax may be estimated on the basis of external indices...". "When records are not provided or are incomplete and insufficient, it is [the Tax Commission's] duty to select a method reasonably calculated to reflect the taxes due. The burden then rests upon the taxpayer to demonstrate...that the method of audit or the amount of the tax assessed was erroneous" (Surface Line Operators Fraternal Organization, Inc. v. Tully, 85 A.D.2d 858).

B. That petitioner has not demonstrated that its gross sales as reported on its Federal income tax returns were correct. The audit findings only determined the taxable percentage of purchases and do not support petitioner's arguments that its gross sales were correctly reported but that its taxable sales were incorrect. Moreover, petitioner did not adequately demonstrate that its test of in-house charge sales indicated a taxable percentage of 41.1 percent. As discussed in Finding of Fact "8", there appear to have been numerous missing charge slips from the month tested, thus rendering the test unreliable for determining an accurate taxable percentage of its sales.

C. That petitioner's taxable percentage test of Drug Guild purchases for a different two week period from the Audit Division's resulted in a 15 percent difference between the two periods. In view of the evidence and testimony

presented by petitioner, an average taxable percentage of 28.1 percent is to be used with respect to Drug Guild purchases. Drug Guild purchases for the test period amounted to \$202,351.00 and 28.1 percent of said amount results in average taxable purchases from Drug Guild of \$56,860.63. The auditor determined average taxable purchases from Drug Guild to be \$74,000.00, thus, taxable purchases for the test period must be reduced by \$17,139.97. The taxable purchases determined by the auditor for the period prior to September 1, 1976 were \$302,978.34, therefore, the correct taxable purchases for that period were \$285,838.37. When the latter figure is divided by total purchases of \$479,933.43, the result is a taxable ratio of 59.56 percent for the pre-September 1, 1976 period. The taxable purchases determined by the auditor for the period after September 1, 1976 were \$297,295.06, therefore, the correct taxable purchases for that period were \$280,155.09. When the latter figure is divided by total purchases of \$479,933.43, the result is a taxable ratio of 58.37 percent for the post-September 1, 1976 period. Petitioner's additional taxable sales are to be determined by applying the taxable percentages as follows:

Purchases (6/1/75 - 8/31/76)	\$ 609,113.95	
Taxable ratio	59.56%	
Taxable purchases	<u>362,788.27</u>	
Markups (pre 9/1/76) 45.84%	<u>166,302.14</u>	
Taxable sales (6/1/75 - 8/31/76)		\$ 529,090.41
 Purchases 9/1/76 - 2/28/79)	 \$1,182,707.33	
Taxable ratio	58.37%	
Taxable purchases	<u>690,346.25</u>	
Markup (post 9/1/76) 46.09%	<u>318,180.59</u>	
Taxable sales (9/1/76 - 2/28/79		\$1,008,526.80
Total taxable sales		<u>1,537,617.21</u>
Less: Pilferage (2.5%)		<u>38,440.43</u>
		1,499,176.78
Less: Bad debt sales		<u>2,407.65</u>
Net taxable sales		<u>1,496,769.13</u>
Less: Reported taxable sales		<u>721,663.00</u>
Additional taxable sales		\$ 775,106.13

D. That petitioner's argument that additional loss leaders should be included in the auditor's markup test to arrive at a markup of 9.6 percent is not supported by the record. As discussed in Finding of Fact "10", such a proposition results in a finding that nearly half of petitioner's sales were of loss leaders. There was no evidence in any form which could support a markup of as low as 9.6 percent, nor a finding that one half of taxable sales were sales of loss leaders.

E. That inasmuch as petitioner could offer no proof as to why, or by how much, the pilferage allowance should be increased to greater than 2.5 percent, it has not met its burden of proving that the audit findings were erroneous and the allowance by the auditor is sustained.

F. That section 1145(a) of the Tax Law, in effect during the period in issue, provides for imposition of a penalty for failure to timely file a return or pay over sales tax unless such delay was excusable. Petitioner offered no reasonable explanation for why completed tax returns were left lying around on desks and then filed late or why such low taxable percentages were consistently used when records were available which clearly indicated a higher percentage was called for. There was, therefore, no excuse for petitioner's delay in paying over the proper amount of sales tax when due.


G. That the petition of GRB Chemists, Inc. is granted to the extent indicated in Conclusion of Law "C"; that the Audit Division is directed to modify the notices of determination and demand for payment of sales and use

taxes due issued November 27, 1979 accordingly; and that, except as so granted,
the petition is in all other respects denied.

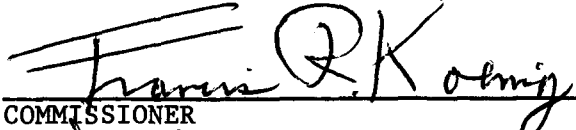
DATED: Albany, New York

STATE TAX COMMISSION

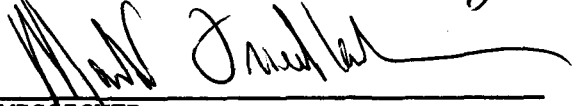
AUG 09 1984



PRESIDENT



COMMISSIONER



COMMISSIONER

P 440 977 393

RECEIPT FOR CERTIFIED MAIL

NO INSURANCE COVERAGE PROVIDED—
NOT FOR INTERNATIONAL MAIL

(See Reverse)

Sent to GRB Chemists, Inc.	
Street and No. 446 Central Ave.	
P.O., State and ZIP Code Cedarhurst, NY 11516	
Postage	\$
Certified Fee	
Special Delivery Fee	
Restricted Delivery Fee	
Return Receipt Showing to whom and Date Delivered	
Return Receipt Showing to whom, Date, and Address of Delivery	
TOTAL Postage and Fees	\$
Postmark or Date	

PS Form 3800, Feb. 1982

P 440 977 394

RECEIPT FOR CERTIFIED MAIL

NO INSURANCE COVERAGE PROVIDED—
NOT FOR INTERNATIONAL MAIL

(See Reverse)

Sent to Arthur Siegel	
Street and No. 342 Madison Ave.	
P.O., State and ZIP Code NY, NY 10173	
Postage	\$
Certified Fee	
Special Delivery Fee	
Restricted Delivery Fee	
Return Receipt Showing to whom and Date Delivered	
Return Receipt Showing to whom, Date, and Address of Delivery	
TOTAL Postage and Fees	\$
Postmark or Date	

PS Form 3800, Feb. 1982