

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition :  
of :  
**BLACKHAT CHIMNEY & FIREPLACE, INC.** : DETERMINATION  
for Revision of a Determination or for Refund of Sales and : DTA NO. 824411  
Use Taxes under Articles 28 and 29 of the Tax Law for the :  
Period June 1, 2006 through August 31, 2008. :

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Petitioner, Blackhat Chimney & Fireplace, Inc., 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, 2006 through August 31, 2008.

A hearing was held before Donna M. Gardiner, Administrative Law Judge, at the offices of the Division of Tax Appeals, 183 East Main Street, Rochester, New York, on May 29, 2013 at 10:30 A.M., with all briefs to be submitted by September 16, 2013, which date began the six-month period for the issuance of this determination. Petitioner appeared by Justin S. White, Esq. The Division of Taxation appeared by Amanda Hiller, Esq. (Michael B. Infantino, Esq., of counsel).

***ISSUES***

I. Whether the Division of Taxation properly issued a Notice of Determination assessing sales and use taxes due for the period June 1, 2006 through August 31, 2008.

II. Whether petitioner has established that reasonable cause exists in order for penalties imposed to be abated.

***FINDINGS OF FACT***

1. Petitioner, Blackhat Chimney & Fireplace, Inc., was a retail business making sales of fireplaces and fireplace equipment located in West Seneca, New York. Petitioner also engaged in contract work. Petitioner performed installations (which qualify as capital improvements) and repairs. Petitioner was owned 100% by Robert Kladke.

2. On October 1, 2008, the Division of Taxation (Division) began an audit of petitioner's sales and use taxes for the period June 1, 2006 through August 31, 2008.

3. The Division determined that petitioner's books and records were insufficient to conduct a detailed audit. Therefore, petitioner elected to have the Division utilize a test period audit methodology in order to determine its sales and use tax liability on its sales and recurring expense purchases.

4. The Division determined petitioner's taxable sales and purchases from the information available, including an analysis of materials used in capital improvements.

5. The agreed upon test period for the audit of sales was December 2006 and January 2008. For the audit of expenses, both for general expenses and for goods sold, the test period was the months of January through August of 2008.

6. To audit the sales, the auditor examined the gross sales in the journals that had been provided by petitioner. The auditor concluded that \$152.09 was underreported for the two test months. This amount was used to calculate an error rate, which when multiplied against petitioner's reported gross sales, resulted in additional tax due on sales for the audit period of \$2,010.53.

7. In reviewing the expenses, the auditor examined petitioner's tendered journal of purchases to determine if tax was properly paid, and he developed a list of exceptions based upon purchases for which he could not satisfy himself that the correct tax had ever been either paid or collected and remitted. For general expense purchases within the test period of January through August 2008, the auditor determined that only two purchases had been untaxed, which resulted in unpaid tax of \$18.78. This amount was projected against a base of reported gross sales for the audit period because petitioner's actual report of these sales made them verifiable. This calculation resulted in additional unpaid tax due on purchases in the amount of \$52.91.

8. The audit of the cost of goods sold was performed using the same method. However, petitioner's accountant had provided documentation for an eleven-month period rather than the agreed upon eight-month test period. The auditor did not notice this at the time of his calculations. The audited tax due for the eight-month test period was \$37,140.21, which was divided by gross sales for the same eight-month period of \$1,450,650.00 resulting in an error rate of 2.5602%. This error rate was multiplied against petitioner's reported gross sales per quarter, which resulted in additional tax due upon the cost of goods sold purchases in the amount of \$104,197.13.<sup>1</sup> Petitioner was given credit for tax already remitted in the amount of \$58,526.71, which resulted in additional tax due of \$45,670.42 for goods sold.

9. The Division issued Notice of Determination L-033642756, dated April 26, 2010, to Blackhat Chimney & Fireplace, Inc., asserting additional sales and use taxes due in the amount of

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<sup>1</sup>Although the Division used eleven months rather than the agreed upon eight months in its calculation of the error rate on the cost of goods sold purchases, the inclusion of the additional months reduced the error rate and, thus, the additional tax asserted is lower (*see Matter of The Humphrey House*, Tax Appeals Tribunal, July 31, 1997). The Division is not seeking a higher tax liability, but rather, admits the computational error and that such error was in favor of petitioner.

\$47,733.86 plus penalties and interest. The auditor testified that penalties were imposed because both additional sales and use taxes were determined to be due without any reasonable cause to justify their abatement as well as the fact that petitioner continued its failure to maintain complete and adequate records of each and every purchase and sale after being audited previously on the same issue.

10. David Gross who is an accountant with over 20 years experience testified on behalf of petitioner. Mr. Gross was brought into the prior audit about halfway through, yet was involved in this current audit throughout the process. Mr. Gross testified regarding the accounting system used by petitioner in its sales tax compliance. Mr. Gross explained that petitioner uses a system called Peachtree accounting system, which has certain limitations. He described that this particular accounting program does not provide for the printing of individual invoices. Although he was able to view certain financials and sales tax reports on the computer system, the detailed backup documentation for the amounts was not available to be printed out.

11. Mr. Gross performed a series of calculations that were designed to estimate more accurately the sales tax liability of petitioner. He explained that he took the total cost of goods sold for the audit period and multiplied that by approximately 60% for each year to come up with a taxable base. He then subtracted out a credit for tax paid on costs of goods that were not used in capital improvement jobs. Then, he subtracted out the tax paid and came up with an estimated figure. Although admitting that his estimation process was not perfect, his goal was to get as close as possible to the correct sales tax liability.

**CONCLUSIONS OF LAW**

A. Petitioner herein elected to a test period audit method and the Division utilized this method as agreed. Estimates by the Division of a taxpayer's liability are acceptable on the principle that "where the taxpayer's own failure to maintain proper records prevents exactness in determination of sale tax liability, exactness is not required" (*Matter of Meyer v. State Tax Commn.*, 61 AD2d 223, 228, *lv denied* 44 NY2d 645).

The rule in these types of cases is that the petitioner has the burden to prove by clear and convincing evidence, that the method of audit used or the amount of tax assessed was erroneous (*Matter of Meskouris Bros. v. Chu*, 139 AD2d 813; *Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858). A taxpayer cannot successfully challenge the Division's determination of taxable sales merely by offering its own estimate of its tax liability (*see Matter of Meskouris Bros. v. Chu*).

B. Petitioner has failed to sustain its burden of proof to show that the amount of tax assessed was erroneous. In fact, petitioner has admitted that it was unable to track its individual transactions and, instead, has presented its own estimate, which it argues is more accurate. Petitioner has not produced any verifiable source documentation to demonstrate that the Division's estimated audit method was otherwise incorrect or unreasonable. Therefore, the assessment by the Division herein is proper.

C. With respect to the issue of penalties, petitioner has failed to demonstrate any basis for abatement. Thus, penalties are sustained.

D. The petition of Blackhat Chimney & Fireplace Inc., is denied and the Notice of Determination L-033642756 dated April 26, 2010 is sustained.

DATED: Albany, New York  
March 13, 2014

/s/ Donna M. Gardiner  
ADMINISTRATIVE LAW JUDGE