

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions :

of :

CHANG LIU JIANG :

DETERMINATION
DTA NO. 826063

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, 2007 through August 31, :
2010.

Petitioner, Chang Liu Jiang, 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, 2007 through August 31, 2010.

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, in New York, New York, on February 18, 2015 at 10:30 A.M., with all briefs to be submitted by May 7, 2015, which date began the six-month period for the issuance of this determination. Petitioner appeared pro se. The Division of Taxation appeared by Amanda Hiller, Esq. (Robert A. Maslyn, Esq., of counsel).

ISSUES

I. Whether a transfer in bulk as defined in Tax Law § 1141(c) occurred creating transferee liability for which petitioner was liable.

II. Whether the Division of Taxation had a rational basis for the issuance of the Notice of Determination to petitioner.

FINDINGS OF FACT

1. On March 1, 2012, petitioner, Chang Liu Jiang, doing business as Sky Wok Chinese Restaurant, entered into a six-year lease agreement with Mr. Banke Tung for a storefront at 315 Utica Avenue, Brooklyn, New York, for the exclusive purpose of operating a Chinese take-out restaurant. The annual rent was \$15,600.00 for the first two years and \$16,068.00 for the four following years. Pursuant to the terms of the lease agreement, petitioner was obligated to purchase his electricity from the landlord.

2. Although not stated in the lease, the premises was fully equipped with the appliances and equipment necessary to operate a Chinese take-out restaurant, which neither party disputed. Petitioner was required to purchase only his food stuffs, packaging and supplies to operate the business. The lease clearly stated that any improvements to the premises became the property of the landlord and that petitioner was entitled to quiet possession of the premises for a defined period only, from March 1, 2012 through February 28, 2018.

3. Petitioner had operated his own restaurant near Eastern Parkway in Brooklyn for five years prior to this venture. He sold that business and did other work for the year immediately preceding the date of the lease. He learned of the turnkey business opportunity at 315 Utica Avenue through Mrs. Tung, who represented to him that her husband could rent him a restaurant to manage. Petitioner was not well acquainted with the Tung family and, when he first learned of the business opportunity, did not know their first names. However, the lease identified the landlord as Banke Tung and the Division's exhibits, including the referral to the bulk sale unit by a compliance agent, identified the prior manager as Fan Chuen Tung, Banke Tung's son.

4. In preparing to start operations, petitioner applied for and received a sales tax certificate of authority. On his application, petitioner stated that he planned on beginning his

business on March 1, 2012, the date his tenancy began at 315 Utica Avenue pursuant to the terms of the lease agreement.

5. On or about November 6, 2012, the Division's Bulk Sale Unit received a written communication from a Tax Compliance Agent, Joseph Harper, that a bulk sale had occurred between Fan Chuen Tung and petitioner on March 14, 2012. Mr. Harper noted that the name of petitioner's business was New Sky Wok Kitchen, while the former business, operated by Fan Chuen Tung, had been called Sky Wok Garden Restaurant. Mr. Harper did not identify the source of his information, listed no equipment or inventory of the business and supplied no information on the sales price of the assets sold or an appraised value of same, except to say the information was not available. His memorandum to the Bulk Sales Unit did not indicate he had visited the premises or spoken with the alleged seller and purchaser. He did list a telephone number for petitioner's business, confirmed by an Internet search engine called "Search Bug," but listed none for Mr. Fan Chuen Tung. Other than listing a date of sale and that the business sold was a restaurant, Mr. Harper's referral to the Bulk Sales Unit contained no details of the sale.

6. On December 4, 2012, the Sales Tax Desk Audit Section, Bulk Sales Unit, sent a letter to petitioner informing him that it had received information that Sky Wok Garden Restaurant had been involved in a bulk sale transaction and that petitioner had been identified as the purchaser. He was instructed to file a form that officially gave the Division notice of the sale and a basis upon which to determine petitioner's liability, if any. He was also cautioned that if he did not respond within 20 days, his liability for tax, penalties and interest would be determined on "all available information." The letter was signed by Leo Kazanjian, a tax technician in the unit.

7. From an affidavit of Mr. Kazanjian and documents included in the Division's bulk sale file, the remainder of the Division's investigation can be discerned. Mr. Kazanjian stated that his unit was informed by Mr. Harper that a bulk sale had occurred in March 2012 between Fan Chuen Tung and petitioner. He noted that no notice of bulk sale had been filed by either the seller or purchaser. After sending the December 4, 2012 letter to petitioner, he received a telephone call from WYCPAS, LLC, an accounting firm that purportedly represented petitioner. The caller informed Mr. Kazanjian that no bulk sale had occurred. The caller was told to provide a power of attorney, a signed lease, utility startup bills, and receipts for inventory.

8. On January 2, 2013, Mr. Kazanjian received a letter from petitioner in a WYCPAS, LLC, envelope, in which he informed the Division that his business was a take-out restaurant located at 315 Utica Avenue in Brooklyn that he leased directly from the landlord. Petitioner stated that he did not pay any consideration or buy the business from the former occupant of the premises. None of the requested documentation was enclosed.

9. Based on his independent analysis, Mr. Kazanjian determined that a bulk sale had occurred because of the following facts:

- a) the two businesses were virtually identical and located at the same address;
- b) the seller and purchaser maintained the same business telephone number;
- c) the assumed business names of the businesses were similar;
- d) the seller's last day in business was February 29, 2012 and the purchaser's first day in business was March 1, 2012, leaving no break in operations;
- e) both businesses employ the same accounting firm;
- f) both businesses reported similar quarterly sales in four quarters; and

g) petitioner failed to provide any documentation on his purchase of the business assets and inventory.

10. Mr. Kazanjian noted that there was an outstanding sales tax assessment against the seller, Fan Chuen Tung, in the amount of \$26,684.75 for tax alone. Since petitioner failed to provide evidence that no bulk sale had occurred or proof of the value of the assets purchased or purchase price of the business, he caused the Notice of Determination to be issued to petitioner in the amount of the seller's outstanding sales tax assessment on January 16, 2013. The Notice of Determination stated in bold print the tax had been estimated.

11. Mr. Kazanjian's affidavit relied on his notes contained in the bulk sales file that were prepared on May 9, 2013. In those notes he stated that based on the evidence before him he believed the assessment issued to petitioner was "fair" and issued "without malice."

12. WYCPAS, LLC, prepared petitioner's sales tax return for the quarter ended August 31, 2012 and appeared on his quarterly sales tax return for the period ended May 31, 2012 and his application for his sales tax certificate of authority as part of the business's mailing address.

13. Petitioner explained that the name of the restaurant was chosen by the landlord and was deliberately similar to the former eatery to attract former clientele. He stated that the premises were equipped with the equipment he needed to operate the restaurant, albeit heavily used and worn. He purchased food inventory and supplies with cash upon starting the business. He claimed the amount he paid his landlord in monthly rent included utilities, thereby obviating the need to open a new utility account, which was consistent with the lease provisions.

14. Petitioner became aware of WYCPAS, LLC, in his discussions with the Tungs and thought it was sensible to use the firm to get his sales tax certificate of authority and file his sales

tax returns since the firm was familiar with the prior business at the location. For his personal income taxes he retained the services of Chan and Company LLC.

15. On August 13, 2013, petitioner and Banke Tung executed a Surrender Agreement whereby petitioner surrendered possession of the premises at 315 Utica Avenue back to Banke Tung.

CONCLUSIONS OF LAW

A. Tax Law § 1141(c) requires the purchaser in a bulk sale transaction to give notice of such sale to the Division at least ten days before taking possession of or making payment for the business assets. Compliance with this provision affords the purchaser protection against becoming liable for the seller's unpaid sales tax liabilities. That is, upon the timely filing of a notification of bulk sale, the Division is obligated to inform the purchaser of the existence of a possible claim for sales and use taxes owing by the seller (20 NYCRR 537.6[a][3]). Once this notice of claim is provided to the purchaser, it is then advised of the existence of such claim of taxes due from the seller and of its personal liability for such taxes to the extent of the greater of the fair market value of the assets transferred or the consideration paid (*see* 20 NYCRR 537.0[c][2]; 537.4[a][1];[c]). Thus, a purchaser may protect itself by placing the consideration to be paid for the transfer in escrow, pending resolution of the Division's claim, so as to be available in the event a liability is determined and upheld. In contrast, if the purchaser fails to file a proper and timely notice of bulk sale, then such purchaser remains personally liable for the sales and use taxes due from the seller.

B. The term "bulk sale" is defined at 20 NYCRR 537.1(a) to mean:

"any sale, transfer or assignment in bulk of any part or the whole of business assets, other than in the ordinary course of business, by a person required to collect tax and pay the same over to the Department of Taxation and Finance."

The term “sale” is defined in Tax Law § 1101(b)(5) to include any *lease to use* or consume tangible personal property, conditional or otherwise, for a consideration. The receipts of such a sale are subject to tax pursuant to Tax Law § 1105(a). A bulk sale can occur even when the purchaser is not required to transfer over to the seller “any sums of money” (*see Matter of Peconic Bay Motors, Inc.*, Tax Appeals Tribunal, September 26, 1991 [Tax Law § 1141(c) applies in the case where the sole consideration received by the seller takes the form of debt relief]).

C. Here, the record established that petitioner learned of an opportunity to operate a Chinese take-out restaurant in a familiar location that had been operating as such a restaurant. With his experience in management, he entered into a lease with the landlord of the property, applied for and received a certificate of authority and commenced operations as soon as possible following the execution of the lease.

The strategy, as credibly testified to by petitioner, was to capitalize on the former restaurant’s name and clientele. The name was changed from Sky Wok Garden Restaurant to New Sky Wok restaurant, an apparent effort to keep old customers, and the business telephone was retained for convenience. Petitioner credibly testified that he never intended to purchase the assets of the business, only lease the space to operate his business.

The record clearly reflects that petitioner leased the premises for a specified consideration and, as part of that transaction, received quiet possession of the property at 315 Utica Avenue. He also received the equipment necessary to operate a Chinese take-out restaurant, i.e., tangible personal property, which was never mentioned in the lease, except to say that petitioner’s use and occupancy would be for the operation of a Chinese take-out restaurant. By operation of Tax Law § 1101(b)(5), under these circumstances a sale occurred. Since it was the “sale, transfer or

assignment in bulk of any part or the whole of business assets,” it constituted a bulk sale (20 NYCRR 537.1[a]). However, contrary to the Division’s conclusion, the seller was not Fan Chuen Tung, the manager of Sky Wok Garden Restaurant, but Banke Tung, the lessor who actually transferred the business assets to petitioner with the premises under the lease agreement. In fact, the lease agreement stated that petitioner leased the premises specifically for a Chinese take-out restaurant and neither party disputed the fact that the premises were provided fully equipped for the operation of a restaurant on March 1, 2012. The Division has offered no evidence of a sale between Fan Chuen Tung and petitioner, whereas petitioner has credibly testified how he came to hear of the opportunity from Mrs. Tung, leased the premises from Banke Tung and received all the equipment for the operation of his business, New Sky Wok Restaurant, from Banke Tung pursuant to the lease agreement. The only bulk sale for which there is any credible evidence in the record occurred as a result of the lease.

The Tax Appeals Tribunal said, “the sine qua non of a bulk sale is a transfer of business assets. . . There is no evidence, testimonial or otherwise, that assets were, in fact, transferred from one entity to the other.” (*Matter of Shanghai Pavilion, Inc.*, Tax Appeals Tribunal, June 10, 2010 [where the Tribunal determined there was no rational basis for the assessment of the petitioner as a bulk sale purchaser when the existence of bulk sale could not be established].)

The Division’s finding of a bulk sale between Fan Chuen Tung and petitioner was the result of a flawed investigation by the Division, which assumed a bulk sale had occurred based on the referral of a compliance agent, Joseph Harper, who apparently had noticed that there had been a change in management at the restaurant located at 315 Utica Avenue. No explanation was given for Mr. Harper’s determination of a bulk sale other than a change in name. The Division never alleged that he visited the restaurant or contacted either the seller or petitioner.

After being informed by petitioner's representatives on several occasions that no bulk sale had occurred and that petitioner had merely taken over from the landlord, the Division decided to hold him liable as a purchaser in bulk from Fan Chuen Tung. The Division's decision was based on seven factors they found compelling:

- a) the two businesses were virtually identical and located at the same address;
- b) the seller and purchaser maintained the same business telephone number;
- c) the assumed business names of the businesses were similar;
- d) the seller's last day in business was February 29, 2012 and the purchaser's first day in business was March 1, 2012, leaving no break in operations;
- e) both businesses employ the same accounting firm;
- f) both businesses reported similar quarterly sales in four quarters; and
- g) petitioner failed to provide any documentation on his purchase of the business assets.

None of the first six factors has any bearing on the transfer of assets between Fan Chuen Tung and petitioner, which the Division insists occurred. With respect to the seventh factor cited, the Division was informed by petitioner that there had been no purchase of assets from Fan Chuen Tung and, therefore, no documentation was provided. Petitioner credibly testified how he assumed possession of the premises and the equipment therein and buttressed his testimony with copies of his lease with Banke Tung and the lease surrender agreement, also with Banke Tung. Since it is determined that a bulk sale occurred pursuant to the lease, the bulk sale seller was Banke Tung. Petitioner's liability pursuant to Tax Law § 1141(c) extends only to the sales and use taxes determined to be due from the seller. The taxes asserted to be due in the Notice of Determination were the sales and use taxes due from Fan Chuen Tung, not Banke Tung. Since it

has been determined that petitioner was the bulk sale purchaser from Banke Tung, he has no liability for the taxes asserted in the notice.

D. Assuming arguendo there had been a bulk sale between Fan Chuen Tung and petitioner, petitioner would not have been liable for the taxes asserted in the Notice of Determination because the Division has not established a rational basis for its issuance, notwithstanding its conclusion that the Notice of Determination was both fair and “issued without malice.”

The Notice of Determination issued to petitioner herein was estimated in accordance with Tax Law § 1138, as plainly stated thereon in bold type. In *Matter of Abbasi* (Tax Appeals Tribunal, June 12, 2008), the Tribunal stated:

“The standard for reviewing a sales tax audit where external indices were employed is as follows. The Division must first request and thoroughly examine the taxpayer’s books and records for the entire period of the proposed assessment. The purpose of the examination is to determine, through verification drawn independently from within these records, whether they are in fact so insufficient that it is virtually impossible for the Division to verify taxable sales receipts and conduct a complete audit from which the exact amount of tax due can be determined. Where the Division follows this procedure, and thereby demonstrates that the records are incomplete or inaccurate, the Division may resort to external indices to estimate tax. The estimate methodology utilized must be reasonably calculated to reflect taxes due, but exactness in the outcome of the audit method is not required. The taxpayer bears the burden of proving with clear and convincing evidence that the assessment is erroneous or that the audit methodology is unreasonable. In addition, considerable latitude is given an auditor’s method of estimating sales under such circumstances as exist in each case (citations omitted).”

In addition, *Abbasi* made it abundantly clear that “the record must contain sufficient evidence to enable the trier of fact to determine whether the audit has a rational basis, as well as specific information identifying the external index employed by the Division in estimating tax liability (see *Matter of Grecian Sq. v. New York State Tax Commn.*, 119 AD2d 948 [3d Dept 1986];

Matter of Spallina, Tax Appeals Tribunal, February 27, 1992; *Matter of Fokos Lounge*, Tax Appeals Tribunal, March 7, 1991; *Matter of Fashana*, Tax Appeals Tribunal, September 21, 1989; *Matter of Savino*, Tax Appeals Tribunal, September 22, 1988).

In *Matter of Basileo* (Tax Appeals Tribunal, May 9, 1991), the Tribunal said:

“We have held that the record must contain information identifying the external index used by the Division to establish a rational basis for the audit methodology employed. We also conclude that the Division must, at hearing, through witnesses or documents, be able to respond meaningfully to inquiries regarding the nature of the audit performed. Such information is necessary in order to provide petitioner with an opportunity to meet its burden of proving such methodology unreasonable. Since the Division was unable to provide such responses at this hearing, we conclude that the audit is without rational basis and the taxpayer sustained its burden to show that the audit methodology was unreasonable (citations omitted).”

This rationale is equally applicable to cases involving the liability of purchasers in bulk sales for the taxes owed by sellers. (Tax Law § 1138[a][3].) In the instant matter, the Division has offered no evidence of the external index it relied upon to establish a rational basis for the audit methodology employed in arriving at the seller’s liability of \$26,684.75. The Division provided no witnesses at hearing and produced no documents to explain the audit methodology used. The affidavit of Mr. Kazanjian did not address the audit methodology, only explaining the basis for his belief that a bulk sale had occurred. Thus, petitioner was never presented with the opportunity to meaningfully question the audit performed or the derivative liability asserted against him by the Division. In short, the record was devoid of sufficient evidence to enable this forum to determine whether the audit had a rational basis (*Abbasi*).

After determining petitioner’s liability as a bulk sale purchaser under Tax Law § 1141(c), it was incumbent upon the Division to identify the external index it used to establish a rational basis for the audit methodology employed that resulted in its assertion that petitioner was

derivatively liable for the full amount of the tax owed by Fan Chuen Tung. Since it did not do so, it must be concluded that there was no rational basis and the taxpayer has sustained his burden to show that the audit methodology was unreasonable. (Tax Law § 1138[a][3]; *Matter of Basileo.*)

E. The petition of Chang Liu Jiang is granted and the Notice of Determination, dated January 16, 2013, is canceled.

DATED: Albany, New York
October 15, 2015

/s/ Joseph W. Pinto, Jr.
ADMINISTRATIVE LAW JUDGE