STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
FLAIR BEVERAGES CORPORATION	:	DETERMINATION DTA NO. 826110
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, 2009 through February 28, 2013.	:	

Petitioner, Flair Beverages Corporation, 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, 2009 through February 28, 2013.

A hearing was held before Catherine M. Bennett, Administrative Law Judge, on September 1, 2015 at 10:30 A.M., in New York, New York, with all briefs to be submitted by January 22, 2016, which date began the six-month period for issuance of this determination. In accordance with Tax Law § 2010(3), for good cause shown, the due date was extended an additional three months upon notice to the parties. Petitioner appeared by Isaac Sternheim & Co. (Isaac Sternheim, CPA). The Division of Taxation appeared by Amanda Hiller, Esq. (Stephanie M. Scalzo, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly imposed penalties on petitioner for failing to file information returns as an alcoholic beverage wholesaler for the period in issue.

FINDINGS OF FACT

1. Petitioner, Flair Beverages Corporation, is an alcoholic beverage wholesaler licensed by the New York State Liquor Authority (SLA) under a 103C liquor license and is located at 3857 9th Avenue, New York, NY. Paul Gagliardi, petitioner's president, estimated that approximately 98% to 99% of petitioner's business involves sales to vendors for resale. Petitioner's sales consist of alcoholic beverages, iced tea, water, juices, ice, and other non-alcoholic beverages.

2. David Viall, a tax auditor in the Division's Audit Investigation Selection Unit, reviews information and provides assistance to taxpayers who have an information return filing requirement, such as in this case. At the hearing, the auditor described legislation enacted in 2009, requiring every alcoholic beverage wholesaler licensed by the SLA that sells alcoholic beverages without collecting sales or use tax to file annual transaction information returns with the Division of Taxation (Division). The new filing requirement covers sales by alcoholic beverage wholesalers primarily to retail vendors for resale.

3. The first information returns required by Tax Law § 1136(i) were due on or before September 20, 2009 and covered the period March 1, 2009 through August 31, 2009. The next information returns were due on or before March 20, 2010 and covered the period September 1, 2009 through February 28, 2010. All subsequent annual transaction information returns are required to be filed on or before March 20th of each year, and cover the period from March 1st of the previous year through February 28th or 29th of the current year.

4. The annual transaction information returns must be filed electronically through the Division's web site. The web site contains instructions describing how to file the "Annual Beer, Wine, & Liquor Wholesalers Transaction Information" return by downloading an Excel

spreadsheet template from a provided link, entering the necessary data, and then uploading the completed file to the Division's online tax system.

5. The record includes the template of a blank Excel spreadsheet that requires provision of the following information for the period covered by the return with respect to each vendor located in New York State to whom the alcoholic beverage wholesaler made a sale without collecting sales or use tax: the vendor's legal name; the vendor's doing business as (DBA) name; the vendor's SLA license address, including the city, state and zip code; the vendor's telephone number; the vendor's mailing address, including the city, state and zip code; the vendor's SLA license number; the vendor's Federal Tax Identification number (EIN); the vendor's New York State Sales Tax Identification number; the year and month of reported sales; and the total monthly net sales amount. Although the Division requests all the information previously described, according to the Division's auditor, there are five required fields of the 16 total fields that need to be completed for the Division to consider the return to be properly completed. The five required fields are the vendor's legal name, the SLA number, the New York Sales Tax ID number, the year and the month of reported sales, and the monthly net sales.

6. The Division uses the annual information returns to scrutinize the sale of alcoholic beverages by wholesalers, such as petitioner, to vendors, and to determine the accuracy of income and sales tax returns filed by vendors to whom sales are made. The auditor conceded that since petitioner's information returns would only report wholesale alcoholic beverages, the information report does not provide the Division with any pertinent information about petitioner's overall business, including its sales of nonalcoholic beverages.

7. On September 14, 2009, petitioner filed a request for a 90-day extension to file the annual transaction information return for the initial filing period of March 1, 2009 through

August 31, 2009. The Division granted the extension and the extended due date for the initial filing period was December 21, 2009. On March 19, 2010, petitioner filed a request for a 90-day extension of time to file the annual transaction information return for the period September 1, 2009 through February 28, 2010. The extension was granted, and the due date for filing that information return was extended to June 21, 2010. However, petitioner failed to file either of the information returns for which the Division had granted 90-day extensions.

8. The Division introduced documents from the auditor's information return folder compiled with respect to petitioner. The management logs contained notes that reflected outreach efforts by several of the Division's tax information aides to petitioner on January 13, 2012, July 26, 2013 and August 7, 2013, essentially as a reminder that information reports were due to be filed with the Division and had not been received.

9. Petitioner did not file information returns for the tax periods ending August 31, 2009, February 28, 2010, February 28, 2011, February 29, 2012, and February 28, 2013. As a result of petitioner's failure to file information returns for the five noted periods, the Division determined that the penalty should be assessed for each period pursuant to Tax Law §§ 1136(i) and 1145(i).

10. The Division issued a Notice of Determination (Notice No. L-039996577-7) to petitioner dated August 15, 2013, assessing penalties in the total amount of $50,000.00 for the tax periods ending August 31, 2009; February 28, 2010; February 28, 2011; February 29, 2012; and February 28, 2013, i.e., $10,000.00 for each period. The computation section of the notice provided, in pertinent part, the following explanation:

> "We're imposing a penalty on you because you haven't filed an information return as required by section 1136(i) of the Tax Law. Because you haven't provided us with your books and records, as we requested, it's necessary for us to estimate the amount of your penalty. Since we can't determine that you owe a lesser amount, we've imposed the maximum penalty allowed by law."

The Division imposed the maximum penalty for each of the five tax periods because it did not know the number of records of alcoholic beverage sales to vendors that petitioner was required to report on each of the information returns.

11. A conciliation conference was thereafter requested, and a conference was conducted by teleconference on December 16, 2013. The conciliation conferee sustained the statutory notice by Conciliation Order No. 258737, dated February 14, 2014.

12. Petitioner filed a petition with the Division of Tax Appeals on February 18, 2014, contesting the Notice of Determination issued herein. The petition asserts that the assessment is arbitrary and does not reflect the correct amount of tax due from the taxpayer.

13. At the hearing it was revealed that the Division did not request books and records from petitioner in order to determine if the penalty in this case should be imposed, and if so, what amount should be assessed.

14. At the hearing, Mr. Gagliardi admitted that petitioner is an alcoholic beverage wholesaler required to file annual transaction information returns. He further admitted that petitioner has not filed all of its information returns.

15. Mr. Gagliardi learned of the requirement to file the information returns sometime in 2009. In an attempt to follow the new procedures, he performed an analysis of what it would take to enter all the sales into the computer, deducting soda, water, deposits included in pricing, sales to exempt organizations and sales to other wholesalers who are not required to collect sales tax, since all the items appear on the same sales receipt. Mr. Gagliardi estimated that petitioner has approximately 300,000 sales transactions each year to vendors, and these are handled by 12 cash registers. Vendor information is accumulated on the computer, but not by the cash registers. Petitioner attempted to transcribe the information and pair the sales transactions with the

customer details. While under an audit, petitioner endeavored to report the transactions as required by the new law. Petitioner spent three months to compile one month of information, with six additional employees working on it and at a cost of $15,000.00 for that effort. Mr. Gagliardi concluded from this effort that it was physically impossible to continually report in the manner requested by the Division with his existing manual system, and so cost prohibitive in the long term that the financial strain placed upon petitioner in trying to electronically file complete annual transaction information returns may force the company out of business.

SUMMARY OF THE PARTIES' POSITIONS

16. Petitioner does not dispute that it failed to file the transaction information returns for the five periods at issue. However, petitioner maintains that the Division erroneously estimated the penalty amounts without requesting and reviewing petitioner's books and records, as it claimed it had in the Notice of Determination. Further, petitioner argues that the Division does not have the right to force a business to purchase a new computer system costing several hundred thousand dollars, thereby putting undue financial and physical burdens on the taxpayer to collect data in order to use the information supplied by the taxpayer for the Division's own policing operations. Petitioner additionally argues that Tax Law §§ 1136(i) and 1145(i) are not only unfair, but illegal and unconstitutional.

17. The Division asserts that petitioner is a party required to file information returns and petitioner has not done so in accordance with the law.

CONCLUSIONS OF LAW

A. Tax Law § 1136 requires the filing of certain returns with the Division. As it concerns this matter, Tax Law § 1136(i) provides, in relevant part, as follows:

"(1) The following persons must file, in addition to any other return required by this chapter, annual information returns with the commissioner providing the information specified below about their transactions with vendors, hotel operators, and recipients of amusement charges:

* * *

(C) Every wholesaler, as defined by section three of the alcoholic beverage control law, if it has made a sale of an alcoholic beverage, as defined by section four hundred twenty of this chapter, without collecting sales or use tax during the period covered by the return, except (i) a sale to a person that has furnished an exempt organization certificate to the wholesaler for that sale; or (ii) a sale to another wholesaler whose license under the alcoholic beverage control law does not allow it to make retail sales of the alcoholic beverage. For each vendor, operator, or recipient to whom the wholesaler has made a sale without collecting sales or compensating use tax, the return must include the total value of those sales made during the period covered by the return (excepting the sales described in clauses (i) and (ii) of this subparagraph) and the vendor's, operator's or recipient's state liquor authority license number, along with the information required by paragraph two of this subdivision . . . .

(2) The returns required by paragraph one of this subdivision must also include, for each vendor, operator, or recipient about whom information is required to be reported under such paragraph, the name and address, and the certificate of authority or federal identification number, and any other information required by the commissioner. The commissioner may, in the commissioner's discretion, require the reporting of less than all the information otherwise required to be reported by this paragraph and paragraph one of this subdivision. . . .

* * *

(3) The returns required by paragraph one of this subdivision must be filed annually on or before March twentieth and must cover the four sales tax quarterly periods immediately preceding such date. Notwithstanding section three hundred five of the state technology law or any other law to the contrary, the returns must be filed electronically in the manner prescribed by the commissioner.

(4) Any person required to file a return under paragraph one of this subdivision must, on or before March twentieth, give to each vendor, operator, or recipient about whom information is required to be reported in the return the information pertaining to that person. The commissioner may prescribe a form to be used to provide the information required to be given by this paragraph.

(5) Nothing in this subdivision is to be construed to limit the persons from whom the commissioner can secure information or the information the

commissioner can require from those persons pursuant to the commissioner's authority under section eleven hundred forty-three of this part or any other provision of law."

B. Tax Law § 1145 imposes penalties and interest for certain failures to file returns or pay tax to the Division as due. Tax Law § 1145(i)[1] provides, in relevant part, as follows:

"(1) Every person required to file an information return by subdivision (i) of section eleven hundred thirty-six of this part who (A) fails to provide any of the information required by paragraph one or two of subdivision (i) of section eleven hundred thirty-six of this part for a vendor, operator, or recipient, or who fails to include any such information that is true and correct (whether or not such a report is filed) for a vendor, operator, or recipient, or (B) fails to provide the information required by paragraph four of subdivision (i) of section eleven hundred thirty-six of this part to a vendor, operator, or recipient specified in paragraph four of subdivision (i) of section eleven hundred thirty-six of this part, will, in addition to any other penalty provided in this article or otherwise imposed by law, be subject to a penalty of five hundred dollars for ten or fewer failures, and up to fifty dollars for each additional failure.

(2) Every person failing to file an information return required by subdivision (i) of section eleven hundred thirty-six of this part within the time required by subdivision (i) of section eleven hundred thirty-six of this part will, in addition to any other penalty provided for in this article or otherwise imposed by law, be subject to a penalty in an amount not to exceed two thousand dollars for each such failure, provided that the minimum penalty under this paragraph is five hundred dollars.

(3) In no event will the penalty imposed by paragraph one, or the aggregate of the penalties imposed under paragraphs one and two of this subdivision, exceed ten thousand dollars for any annual filing period as described by paragraph three of subdivision (i) of section eleven hundred thirty-six of this part.

(4) If the commissioner determines that any of the failures that are subject to penalty under this subdivision was entirely due to reasonable cause and not due to willful neglect, the commissioner must remit the penalty imposed under this subdivision. *These penalties will be determined, assessed, collected, paid, disposed of and enforced in the same manner as taxes imposed by this article and all the provisions of this article relating thereto will be deemed also to refer to these penalties.*" (Emphasis provided).

---

[1] There are three versions of Tax Law § 1145(i). This is the second version, which was added by Laws of 2009 (ch 57, pt V-1, subpt G eff April 7, 2009), and appears to be the only one directly related to the returns required under Tax Law § 1136(i)(1)(C).

C. Petitioner contends that Tax Law §§ 1136(i) and 1145(i) are unconstitutional because undue financial and physical burdens are placed upon alcoholic beverage wholesalers such as itself, by requiring them to file the information returns in issue, and penalizing them for failure to do so. Petitioner essentially challenges the constitutionality of Tax Law §§ 1136(i) and 1145(i) on their face.

It is well settled that the Division of Tax Appeals lacks jurisdiction to consider claims alleging that a statute is unconstitutional on its face (***see Matter of A&A Service Sta., Inc.***, Tax Appeals Tribunal, October 15, 2009; ***Matter of R.A.F. General Partnership***, Tax Appeals Tribunal, November 9, 1995) and at the administrative level, statutes are presumed to be constitutional (***see Matter of Lunding v. Tax Appeals Trib.***, 218 AD2d 268 [1996], ***revd*** 89 NY2d 283, 287 [1996], ***cert granted*** 520 US 1227 [1997], ***revd*** 522 US 287 [1998]). It is noted that the constitutionality of Tax Law §§ 1136(i) and 1145(i) has already been decided in ***Empire State Beer Distrib. Assn., Inc. ex rel. Alcoholic Beverage Wholesalers v. Patterson*** (No. 09 CIV. 10339 DAB, SD NY, [Mar. 1, 2010], 2010 WL 749828). In ***Empire***, the Court ruled that Tax Law §§ 1136(i) and 1145(i) did not violate the plaintiff's substantive due process, equal protection, and fourteenth amendment rights, since there was a rational basis for the amendment to Tax Law § 1136 and its implementation schedule. The Court concluded that a rational basis for Tax Law § 1136(i) exists in these provisions as a means of collecting information from liquor wholesalers in order to verify the accuracy of tax reports from retailers, who frequently operate as cash businesses, and found nothing irrational about the added burden on wholesalers to do so. The Court also ruled that the statutes do not violate the Dormant Commerce Clause doctrine, concerning any impact upon interstate commerce.

The Division of Tax Appeals may, however, determine whether tax statutes are constitutional as applied (***Matter of Eisenstein,*** Tax Appeals Tribunal, March 27, 2003, citing ***Matter of David Hazan, Inc.***, Tax Appeals Tribunal, April 21, 1988, ***confirmed*** 152 AD2d 765 [1989], ***affd*** 75 NY2d 989 [1990]). The taxpayer bears the burden of proving that a statute, as applied, is unconstitutional (***Matter of Brussel***, Tax Appeals Tribunal, June 25, 1992).

In the present matter, petitioner has offered no evidence that it was treated any differently than other taxpayers, similarly situated, in the application of Tax Law §§ 1136(i) and 1145(i), and therefore it has failed to meet its burden of proof in this regard. As such, any challenge to the constitutionality of the statutes as applied has no merit.

D. In the instant matter, the Division assessed penalties under Tax Law §1145(i) in the total amount of $50,000.00 for the tax periods ending August 31, 2009; February 28, 2010; February 28, 2011; February 29, 2012; and February 28, 2013 because petitioner failed to file information returns for such periods that were required to be filed pursuant to Tax Law § 1136(i). Petitioner, an alcoholic beverage wholesaler licensed by the SLA, does not dispute that it failed to file five information returns for the periods at issue. However, petitioner contends that the Division erroneously estimated the penalty amounts without requesting and reviewing petitioner's books and records, as it claimed it had in the Notice of Determination.

Tax Law §1145(i) must be discussed in terms of its two components, i.e., Tax Law §§ 1145(i)(1) and (2). Tax Law §1145(i)(1) imposes penalties on a person required to file an information return who fails to provide any of the information required on the return, fails to include information on the return that is true and correct, or fails to provide to each affected vendor (by a designated date), the statement that informs each vendor of the same information reported to the Division. The information required on the return is set forth in Finding of Fact 5.

The auditor delineated the five fields that he claimed are the only ones required for a proper filing, as follows: the vendor's legal name, the SLA number, the New York Sales Tax ID number, the year and the month of reported sales, and the monthly net sales. However, in fact, any return after the first six-month return for the period ending August 31, 2009, would not be considered properly filed unless it contained all 16 fields as set forth in the sample Excel spreadsheet submitted into evidence by the Division at the hearing (***see*** Division's Exhibit I). For a failure to provide any item of information, a vendor would be subject to a penalty of $500.00 for 10 or fewer failures, and up to $50 for each additional failure (Tax Law § 1145[i][1]). The Division claimed it did not know how many failures were made by petitioner, since petitioner failed to file any information returns. In other words, the Division could not determine how many separate items of information had been omitted by petitioner, and as a result, effectively estimated the number of failures, resulting in a penalty to be the greatest amount allowed by law, $10,000.00 per filing period. The Notice of Determination, bearing an estimate of the penalties due, was issued to petitioner premised upon petitioner's failure to provide the Division with its books and records "as we requested." It is quite clear from the record, including the auditor's admission, that the Division never requested petitioner's books and records, never examined petitioner's books and records, never made a determination of whether petitioner's books and records could have provided the Division with the information it sought, and never attempted to compile from petitioner's records the information it sought.

Tax Law § 1145(i)(4) states that penalties will be determined in the same manner as taxes imposed by Article 28. Thus, the principles that guide the determination of tax due when a return is not filed, incorrect or insufficient, should be similarly applied to the determination of penalties, including principles governing the methods of estimation of tax due. When a sales tax return is

not filed, or is incorrect or insufficient, the amount of tax due can be determined from the information available, and may be estimated (Tax Law §1138[a][1]). The well-established standard for reviewing a sales tax audit where estimates, i.e., external indices, are employed was set forth in ***Matter of Your Own Choice, Inc***. (Tax Appeals Tribunal, February 20, 2003) as follows:

> "To determine the adequacy of a taxpayer's records, the Division must first request (***Matter of Christ Cella, Inc. v. State Tax Commn.***, [102 AD2d 352, 477 NYS2d 858] ***supra***) and thoroughly examine (***Matter of King Crab Rest. v. Chu***, 134 AD2d 51, 522 NYS2d 978) the taxpayer's books and records for the entire period of the proposed assessment (***Matter of Adamides v. Chu***, 134 AD2d 776, 521 NYS2d 826, ***lv denied*** 71 NY2d 806, 530 NYS2d 109). The purpose of the examination is to determine, through verification drawn independently from within these records (***Matter of Giordano v. State Tax Commn.***, 145 AD2d 726, 535 NYS2d 255; ***Matter of Urban Liqs. v. State Tax Commn.***, 90 AD2d 576, 456 NYS2d 138; ***Matter of Meyer v. State Tax Commn.***, 61 AD2d 223, 402 NYS2d 74, ***lv denied*** 44 NY2d 645, 406 NYS2d 1025; ***see also***, ***Matter of Hennekens v. State Tax Commn.***, 114 AD2d 599, 494 NYS2d 208), that they are, in fact, so insufficient that it is 'virtually impossible [for the Division of Taxation] to verify taxable sales receipts and conduct a complete audit' (***Matter of Chartair, Inc. v. State Tax Commn.***, 65 AD2d 44, 411 NYS2d 41, 43; ***Matter of Christ Cella, Inc. v. State Tax Commn.***, ***supra***), 'from which the exact amount of tax due can be determined' (***Matter of Mohawk Airlines v. Tully***, 75 AD2d 249, 429 NYS2d 759, 760)."

Inasmuch as the Division failed to even make a basic request for petitioner's books and records, the Division's use of an estimated method to determine the penalties was grossly improper. Accordingly, the penalties imposed under Tax Law § 1145(i)(1) derived from such a flawed method, lack a rational basis, are erroneous and must be cancelled.

E. Tax Law §1145(i)(2) provides for the imposition of penalty of not less than $500.00 but up to $2,000.00, for each failure to file an information return within the required time frame. There is no dispute that petitioner did not file the returns in issue. However, petitioner put forth substantial effort to determine if it could readily comply with the Division's TSB-M-09(10)S,

given its existing manual system. Petitioner sought the assistance of his CPA and performed an analysis of what resources it might take to enter approximately 250,000 to 300,000 transactions per year into a computer, deducting soda, water, deposits, and sales to exempt organizations and others not from whom it is not required to collect sales tax. Petitioner did not simply ignore the filing requirement, but with great effort found it physically impossible to perform the tasks and present the information as requested. Accordingly, the minimum penalty of $500.00 per information return that petitioner failed to file will be imposed, for a total of $2,500.00.

F. The petition of Flair Beverages Corporation is hereby granted to the extent of Conclusions of Law D and E, and the Notice of Determination, dated August 15, 2013, is modified in accordance with this determination.

DATED: Albany, New York
September 29, 2016

/s/ Catherine M. Bennett
ADMINISTRATIVE LAW JUDGE