

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition :  
of :  
**MILANO AND SON JEWELRY, INC.** : DETERMINATION  
for Revision of Determinations or for Refund of Sales : DTA NOS. 827296  
and Use Taxes under Articles 28 and 29 of the Tax Law : AND 827297  
for the Period September 1, 2010 through August 30, 2013. :  
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In the Matter of the Petition :  
of :  
**IOSIF ILYABAYEV** :  
for Revision of Determinations or for Refund of Sales :  
and Use Taxes under Articles 28 and 29 of the Tax Law :  
for the Period September 1, 2010 through August 30, 2013. :  
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Petitioners Milano and Son Jewelry, Inc. and Iosif Ilyabayev filed petitions for revision of determinations or for refund of sales and use taxes under articles 28 and 29 of the Tax Law for the period September 1, 2010 through August 30, 2013.

A consolidated hearing was held before James P. Connolly, Administrative Law Judge, on November 2 and 3, 2017, at 10:30 a.m. in New York, New York, and continued to completion on January 3, 2018, at 9:30 a.m. in Albany, New York, with all briefs to be submitted by June 29, 2018, which date commenced the six-month period for the issuance of this determination.

Petitioners appeared by Leibowicz & Ahroni (Barry Leibowicz, Esq., and Scott Ahroni, Esq., of counsel). The Division of Taxation appeared by Amanda Hiller, Esq. (M. Greg Jones, Esq., of counsel).

***ISSUES***

I. Whether the Division of Taxation was entitled to estimate the audit liability of petitioner Milano & Son, Inc., on the ground that its books and records were not an adequate basis on which to perform an audit.

II. Whether, if the Division was entitled to estimate the audit liability of petitioner Milano & Son, Inc., petitioners have established that the indirect audit methodology used by the Division of Taxation was not reasonably calculated to reflect the correct amount of tax due, or that there were errors made in the application of such audit methodology.

III. Whether petitioner Iosif Ilyabayev was properly subjected to liability as a person under the obligation to collect and remit sales and use taxes on behalf of petitioner Milano & Son Jewelry, Inc.

IV. Whether petitioners have established any basis justifying reduction or cancellation of the penalties assessed.

***FINDINGS OF FACT***

1. Petitioner Milano and Son Jewelry, Inc. (Milano), is a jeweler operating two booths on the second floor of the Tri-County Jewelry Exchange (Tri-County) in Levittown, New York. Petitioner Iosif Ilyabayev is the president and owner of the company. Milano sold diamonds and gold jewelry (new gold) and bought gold jewelry from its customers (old gold) for resale to gold refiners. At the time of the audit, there were about 30 other jewelers operating booths at Tri-County, about 15 of which also bought old gold. Tri-County is known as a place to buy and sell gold. The booths at Tri-County were as close as 50 feet apart.

2. Milano is required by law to maintain a record of its purchases of old gold in order to

assist the police in investigating thefts of gold jewelry. The collection of these records is known as a police book. For each purchase of old gold, the police book describes the jewelry involved and identifies the purchaser and the purchaser's address.

3. The Division performed an audit of Milano for the periods September 1, 2010 through August 30, 2013 (periods at issue). The Division's auditor, Stephanie Williams, first conducted an unannounced survey of Milano's operations. She found that Milano occupied two adjacent booths, both selling a large assortment of jewelry. One of the booths had a (POS) system and the other had a punch key register. According to the auditor, a POS system had an electronic database that permitted invoices to be printed at any time.

4. Ms. Williams mailed an audit appointment letter to Milano, dated September 30, 2013, which required Milano to provide "any and all documentation in auditable form and electronic form (if available) which supports the sales and use returns as filed." Attached to the letter was a request for books and records, asking Milano to produce, among other things, its sales tax returns, Federal income tax returns, general ledger, general journal and closing entries, "sales invoices," bank statements, and "cash receipts journal – including sales journal, if applicable." The auditor did not make any additional written requests, but she testified that she made additional oral requests for records. She did not specify the contents of those requests in her testimony and no oral requests are documented in the audit log.

5. On November 8, 2013, the auditor had an initial meeting with Milano's representative at the time, Roman Izyayev. Mr. Izyayev provided the auditor with the general ledger, sale receipts booklets for petitioner's sales of new gold, police books, bank statements, gold refinery invoices, and purchases for retail information. The sales receipts booklets contained "slips" used

for individual sales, with 50 to a booklet. Milano did not produce any sales journal or daily activity log. In her entry in the audit report's log of contacts and comments (form DO-220.5) (audit log) for November 8, 2013, the auditor indicated that the sales receipts "are not in sequential order," some barely have a description, [they] lack customer names, and "the dates are not in order." The auditor analyzed the sales receipts booklets for the period March 1, 2013 through May 31, 2013 and determined that the total amount of the sales shown on the invoices (\$82,946.98) was less than the gross sales reported on Milano's sales tax return for that quarter (\$90,189.34). The auditor's November 8, 2013 entry in the audit log concluded that the sales receipt booklets "are deemed inadequate (sic) for sales tax purposes." The auditor did not note the number of sales receipt booklets; nor does the audit file contain any copies of the individual receipts or any description of the invoice sequences used in quarters other than the one tested. The auditor testified that she asked if Milano had additional sales receipts booklets and was told that it did not.

6. Review of the auditor's schedule of her test of the sales receipts booklets for the March 1, 2013 through May 31, 2013 period confirms the auditor's finding that the sales receipts booklets were not used in sequential order. During the quarter, Milano used six widely-diverging receipt booklets: three six digit series beginning, respectively, 2472, 2479, and 2480; two five-digit series beginning 799 and 801; and a four digit series beginning 56. On some days up to three of these series were used to memorialize sales, such as April 4, 2013, when the 2472, 799 and 56 series were used. The auditor treated all of the sales shown on the sales slips as taxable.

7. The auditor testified that she reviewed all of the sales receipts booklets. She sorted them into sales tax quarters and then chose to test the quarter that "was the most sequential," had

the “most booklets out of all.” According to the auditor, because the booklets used were not sequential, she could not be sure she had all of the booklets that Milano had used during the audit period. The field audit report (DO-1637.2) summed up the state of the sales receipts as follows:

“Sales records were deemed to be inadequate because vendor did not maintain adequate sales invoices/documentation. The sales receipts were not in sequential order, no detail descriptions, no customer name, majority of the receipts were not legible. Records were not in auditable condition. The Sales records did not allow the opportunity to trace any transaction back to the original source or forward to a final total. The Sales accounting records were not in an auditable condition. There were not adequate internal control procedures in the Sales portion of the business operation.”

8. To calculate tax due, the auditor determined the amount of Milano’s purchases of jewelry available for retail sale and then applied a markup factor derived from Milano’s own records. As a first step in determining Milano’s purchases available for retail sale, the auditor accepted Milano’s total purchases of jewelry of \$4,142,961.31 from its general ledger “Purchases-Resale Items” account. The auditor also accepted the figure provided by Mr. Izyayev for Milano’s purchases of old gold as \$1,411,068.00, made up of Milano’s general ledger account for purchases from the public of \$1,282,161.00 and \$128,907.00 from Milano’s account for “total withdrawals from the public.”<sup>1</sup> Subtracting the old gold purchases of \$1,411,068.00 from Milano’s total purchases of jewelry of \$4,142,961.31 yielded purchases for retail sale of \$2,731,893.31. To determine the total receipts received by Milano as a result of selling that amount of jewelry, the auditor applied a 49.97% markup rate. The markup percentage was derived by averaging the markup on 20 items of jewelry from Milano’s inventory. Milano picked out the jewelry items to be used for the markup and supplied both the wholesale and retail prices

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<sup>1</sup> The parties provided no explanation as to what this “withdrawal from public” account represented, and in what way it was distinguishable from Milano’s purchases of old gold from the public.

of the jewelry to the auditor. Applying that markup percentage to \$2,731,893.31 worth of jewelry purchased for resale led to total audited sales of \$4,097,020.40. Subtracting out reported taxable sales of \$1,132,165.00 led to audited additional sales of \$2,964,855.40 and, in turn, \$255,718.72 in additional tax due. The audit report notes that “[u]nder no circumstances was the tax due calculated using other sources or internet data, only records provided by the taxpayer.”

9. On May 16, 2014, the auditor met with Mr. Izyayev and George Libner, another representative of Milano. The audit log shows that Mr. Izyayev claimed that Milano “threw in extra inventory at the end of the year to the refineries” and that, therefore, the auditor should have used the full amount paid by Milano’s refiners as the value of the old gold that needed to be deducted from Milano’s total purchases to derive Milano’s purchases used for retail sales. According to Mr. Izyayev's calculations presented at the meeting, subtracting the \$1,282,161.00 amount shown in the general ledger for “purchases from public” from Milano’s total jewelry purchases of \$4,142,961.31 and subtracting \$115,000.00, which he described as an “Adjustment for inventory & A/P 2010,” and \$128,907.00, as “withdrawals from the public” yields “net purchases” of \$2,616,893.31, of which amount \$769,550.00 was used for retail sales, while the remaining amount of the net purchases was sold to the refineries. The auditor testified that she asked Mr. Izyayev for documentation to substantiate his assertion about some inventory being sold to the refineries, but was not given any, which is consistent with the audit log entry for the meeting.

10. The auditor compiled a month by month total of Milano’s invoices to the gold refineries, which totaled to \$3,108,952.14 for the audit period, and thus a monthly average over the 36 months of the audit period of \$86,359.78. The monthly transcription in the audit file

reveals the following averages for December and January of each year in the audit period:

Month	December	January	Average
December, 2010- January, 2011	\$66,411.00	\$54,247.56	\$60,329.28
December, 2011- January, 2012	\$205,833.00	\$153,959.00	\$179,896.00
December, 2012- January, 2013	\$43,652.00	\$87,862.00	\$65,757.00

While December, 2011 and January 2012 were the months with the highest invoice amounts for 2011 and 2012, for the four months of the audit period in 2010, October was the month with the highest amount of sales, while for the eight months of 2013 in the audit period, April had the highest total. At hearing, petitioners provided no explanation as to why, if sales of new gold to the refineries occurred at the end of each year, there was no consistent increase in sales to the refineries in December or January.

11. After Mr. Izyayev continued to disagree with the proposed audit results based on the amount of Milano's total purchases that the auditor was treating as sold at retail (the difference between the amount determined by the auditor as attributable to purchases of old gold [\$1,411,068.00] and the amount paid by the refineries according to the invoices supplied by Milano [\$3,108,952.14]), the auditor decided to research on the internet the average markup jewelers earned on purchases of old gold from consumers and sold to refiners in order to determine whether the difference between these two amounts could be explained by Milano's markup on its sales of old gold to refiners (confirmation test). As a result of that research, the auditor determined that a jeweler on average pays 40% of the spot value of the gold content of an item of old gold (average payout percentage of jewelers) and is able to sell the item of old gold to

a refinery at 95% (average payout percentage of refineries). She concluded that the resulting 55% markup relative to the spot price of old gold would confirm that Milano's purchase of \$1,411,068.00 in old gold, per the police books, would explain the \$3,108,952.14 amount of Milano's sales to refineries, according to the following analysis:  $\$1,411,068.00$  (purchases of old gold derived from the analysis of the police books, as adjusted by information supplied by the representative)  $\div$  40% (markup derived from the auditor's research) =  $\$3,527,670.00$  X 95% (average payout percentage of refineries, according to the auditor's research) =  $\$3,351,286.50$ , which exceeds  $\$3,108,952.50$ , the total of Milano's invoices for sales to the refineries.

According to the audit log entry for September 23, 2014, in the auditor's view, this analysis showed that the revenue Milano received from the refineries could be explained by the old gold it sold to the refineries. The audit log entry concluded with a note indicating that the above analysis was "not used to calculate the tax due. The tax due was derived from using the taxpayers [sic] records."

12. The audit file contains printouts from a total of seven websites that the auditor considered in determining the average payout percentage of jewelers and the average payout percentage of refineries. Only two bear on the average payout percentage of jewelers, while several discuss the average payout percentage of refineries. The auditor testified that she looked at other websites, but chose to print out information from only a handful and did not record the URLs of the other websites she reviewed. Based on her internet research, she concluded that jewelers will pay anywhere from 30% to 40% of the spot value of gold in the old gold they are purchasing and then sell the old gold to refineries for 95% to 99% of the value of the gold in the jewelry items.



13. One of the websites the auditor used was [www.agrgoldbuyers.com](http://www.agrgoldbuyers.com). The auditor included a two-page excerpt from the website in the audit file. The first page of the print-out has a banner across the top referencing “American Gold Refinery,” and lists a New York City address for the company. As pertinent, the printout in the audit file from that website states the following:

“The major difference between selling your gold to a jeweler, pawn shop or to an on-line gold buyer is that they pay 30-50% less than a reputable and trusted gold refinery with decades of experience. While their (*sic*) are some (an [*sic*] I mean one or 2) high paying gold buyers on the internet, when you factor in the ‘convenience fee’ meaning, (*sic*) the percentage they take off to use their service, American Gold Refinery, (*sic*) meets and exceeds their prices that they pay out on all levels.”<sup>2</sup>

This website, which lists no author, advises consumers that, in order to get the most for their old gold, “keep your gold separated in terms of carats, don’t mix the 10k with the 18k etc, because they sometimes will go with the lowest carat and pay that for all.”

14. A second website the auditor used was “[www.make-money-gold.com](http://www.make-money-gold.com),” from which she retained a single page for the audit file. That page states the following in part:

“Unscrupulous gold dealers like the ones that advertise on radio and TV ask you to mail your gold to them. They typically pay between 10% and 20% of the value of gold. Most pawnshops pay about 30% to 35%. \* \* \* Legitimate dealers pay between 40% and 65%. 40% to 65% may seem low to you, but remember, the gold you buy has to be smelted, refined, assayed and poured into ingots before it can be resold. Refiners who do this will pay you between 85% and 92% of the spot price of gold.”

Elsewhere the website states that “most legitimate gold dealers” pay 50% of the spot value of the gold content in old gold. The purpose of this website appears to be to promote a book on buying and selling gold by one “Skip McGrath,” as a box in the middle of the page contains, in bold

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<sup>2</sup> The auditor’s schedule A inaccurately paraphrases this article as stating “the major difference between selling to a jeweler is they pay 30-50% less than a reputable and trusted gold refinery.”

font, an endorsement of the book, and much of the text of the page is devoted to explaining how to make money in the “gold business.” At hearing petitioners introduced a printout showing the same URL as the printout used by the auditor, which included the language quoted above and also promoted Skip McGrath’s book on selling gold. The last page of that printout included a disclaimer. The disclaimer stated the following;

“New Federal Trade Commission (FTC) regulations effective in January 2010 require that if I state any amount of money I have made . . . , then I have to state the ‘average’ amount of money that everyone who bought this book made. Well, as you can imagine, I would have no way of knowing that!” \* \* \* So to comply with the law, let me say that although myself and other people have made differing amounts of money with these methods: ‘The ‘average’ person who bought the book made less than one-cent (0.01).”

15. The Sales Tax Field Audit Manual provides that an auditor should document in the field audit record all communications and correspondence with the taxpayer. The auditor’s section head, Mr. Robert Wynne, testified that an audit file should contain documentation of anything significant to the audit, including record requests and documents reviewed. The auditor testified that all record requests are supposed to be in writing.

16. As a result of the audit, the Division issued to Milano a notice of determination (notice number L-042258115), dated December 8, 2014, asserting \$255,718.72 in additional tax due, plus interest and penalty, for the periods at issue. Similarly, the Division issued a notice of determination (notice number L-042264487), dated December 9, 2014 to Mr. Ilyabayev, as a person required to collect sales tax on behalf of Milano, asserting the same amount of tax, penalty and interest, for the periods at issue.

17. At hearing, petitioners presented the testimony of Yana Shnaider, a third-year law student employed by Mr. Leibowicz’s law firm. At Mr. Leibowicz’s request, Ms. Shnaider

researched on the internet “how authorities go about pricing gold and different . . . percentages of gold.” She did the research over more than five days, but could not recall how much time she spent on the research each day. Among the authorities she came across were the following:

(a) a 2008 article from the Consumer Reports website. Consumer Reports is a magazine published by the Consumer Union, which is a nonprofit organization. The article is a one-paragraph “Q & A” on selling gold, in which the question is whether a consumer with gold to sell should patronize one of the companies advertised on TV as buying gold. The answer to the inquiry is as follows:

“Maybe not. When Consumer Reports Money Adviser compared what one of those companies offered for a gold band a couple of years ago with what a local jeweler and an on-line gold buyer would pay, the TV company paid a much lower price. Instead, take your gold to a reputable jeweler in your area for an appraisal. Note the carat of the metal, and ask the jeweler to tell you the weight in pennyweights or troy ounces. Use this online calculator to figure out the value based on the price of gold that day. Then quickly (because prices fluctuate) call several jewelry or coin stores and ask how much they pay for gold. Aim to get about 85 percent of what you calculated it’s worth.”

The article does not provide the name of the author of the article or the author’s source of knowledge for the information provided in the last sentence of the Q & A.

(b) a print-out from the website “Goldcalc.com.” In the course of describing different types of buyers of old gold, this website states the following:

“3. **Local Jewelers** or pawn shops often offer competitive (sic) bids for your scrap gold. But also understand that shop owners must pay overhead (rent, utilities, advertising, etc.). When you’re selling to a jeweler or pawn shop, you’re also paying for the *convenience*. This is considerably less work than selling on an on-line auction site. A range between 70% to 85% of melt value is a reasonable expectation from this type of buyer.”<sup>3</sup>

The printout does not list the name of the author or the basis of that person’s knowledge of the gold market.

(c) a print-out from [www.usedjewelrybuyer.com](http://www.usedjewelrybuyer.com). This website purchased used gold

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<sup>3</sup> This print-out is substantively the same as a print-out that Mr. Leibowicz obtained from the Division as part of a Freedom of Information Law (FOIL) response transmitted by a letter dated June 26, 2015 from the Division’s Records Access Officer.

jewelry, and included a “mail in” service. The website opined that a consumer with a gold jewelry item to sell could expect to obtain 80% to 85% of the item’s true gold value. The website is owned by Mr. Brian Hill and bears his signature.

(d) an article from [www.bankrate.com](http://www.bankrate.com). According to its first page, the article was by Jennie Phipps and it first appeared in a March 2008 edition of the magazine Smart Money. With regard to the question of how much a consumer can expect from selling old gold, the article advises that the consumer should “expect that the dealer will keep some for himself – at least 10% and maybe as much as 30%.” The article supplies no information about Ms. Phipps’s background or the resources she used to compile the information. Elsewhere it advises consumers to “[s]hop around. You may find great differences in the offers you get for your gold.”

18. As further proof of the average payout percentage of jewelers, petitioners arranged to have six gold jewelry items of known gold content sold to a number of other jewelers at Tri-County on June 22, 2017 (Tri-County investigation). As a first step, Mr. Ilyabayev had six pieces of jewelry appraised for their gold purity by American Appraisal Association (AAA), an organization with offices in New York City’s Diamond District that he chose randomly, having no prior relationship with them. AAA issued appraisals for each item. Each appraisal had an appraisal number, a picture and a description of the jewelry item, lists its “Metal Purity” and “Total Weight,” and bears the signature of a “GIA Gemologist.” Each has the same terms and conditions, including the following:

“[AAA] is in the business of conducting jewelry appraisals and full service laboratory reports. The information stated in this certificate/report is the result of laboratory examination with the described items present during examination. The gemologist used all standard and necessary laboratory grading tools: microscope, jewelry loupe, color grading chart, color scale, master stone set, millimeter gauge, fluorescence lamp, leverage gauge, ruler, etc. . . . This report is in fact a gemological opinion and does not state a fact. . . . This document is for estimating the retail, wholesale, and liquidation values in order to obtain insurance.”

Mr. Ilyabayev testified that GIA is a certifying authority for jewelers and that its permission is needed to “certify everything.”

19. By determining the purity of the gold in the six items of jewelry and the gross gram weight of the items, the AAA appraisals establish that the weight of the gold in the six items of gold jewelry was 16.974739 grams.

20. To calculate the value of that amount of gold on June 22, 2017, petitioners used that day's closing price of the spot value of gold shown on the Kitco.com website. Mr. Ilyabayev testified that Kitco.com is a reputable place to obtain the spot value of gold. Furthermore, the website was cited as a "good source of recent gold price data" in a April 2013 blog post on the New York Times blog *Economix*. The Division has not disputed that Kitco.com is a reliable source of the spot value of gold and it is accepted as such herein. The spot value of gold on June 22, 2017 was \$1,251.60 per troy ounce, which is the equivalent of \$40.239844 per gram.<sup>4</sup> At that spot price, the value of the 16.974739 grams of pure gold (24K) in the six items of jewelry was \$683.06.

21. Ms. Shnaider conferred with Mr. Ilyabayev and obtained the six jewelry items from him on June 21, 2017. The next day, Ms. Shnaider took the six items of jewelry to Tri-County, where she approached 11 of the jeweler booths, said that she wanted to sell the jewelry, and asked them to price it for her. Ms. Shnaider had worked in a jewelry store previously, and had sold old gold in the past. According to her testimony, at Tri-County, "there were only certain vendors that were gold buyers. They were certified gold buyers. So those were the ones I chose and visited." Of those, she said she visited "the majority of them, missing only "two, maximum three." She missed them because "they either connected to ones that I already did visit, so one vendor might have two groups, or there was no one there." She said she identified that they were

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<sup>4</sup> A troy ounce of gold is equal to 31.1035grams.

certified gold buyers from the signs on their booths. According to Ms. Schnaider, to be “certified” means they “are allowed to buy your gold and give you money for it.” Petitioners introduced a map of the floor at Tri-County, which lists 31 booths. Petitioners also introduced pictures of 27 booths at Tri-County, seventeen of which had signs indicating that they bought gold. None of the signs uses the word “certified.”

22. When Ms. Schnaider obtained a pricing estimate, she recorded the interaction with the jeweler on her smart phone and wrote the offer she had received on the back of the jeweler’s business card, except in one instance where the jeweler did not have a business card. After each interaction with a jeweler, she generally made a voice recording, in which she noted the name of the jeweler booth and the name of the person at the booth with whom she talked. Starting that same day, she prepared a spreadsheet (the exhibit 41 table), which compares the offers she got for the six pieces of gold jewelry from the jewelers at Tri-County against the value of the gold in those items based on their gold purity and weight, taking into account the spot value of gold on that day. She later burned the recordings to a CD and had it transcribed. Petitioners submitted both the transcript (exhibit 46 transcript) and CD into evidence at the hearing. At hearing, Ms. Schnaider testified that she double-checked the information on the exhibit 41 table against the information on the business cards and recordings and that the transcript has everything that is on the CD.<sup>5</sup>

23. There are discrepancies between the business cards, the exhibit 46 transcript, and the

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<sup>5</sup>As a result of this methodology, the names of the jewelry businesses from which Ms. Schnaider obtained pricing estimates are not in the recordings themselves, but the name of the recording for each encounter on the CD is the name of the business and/or the name of the person at the business with whom Ms. Schnaider dealt. The name of the business and the name of the person at the business with whom Ms. Schnaider dealt is also indicated in the exhibit 46 transcript. Portions of the CD recordings are not audible, as reflected in the exhibit 46 transcript. Review of the recordings did not reveal any discrepancies between the exhibit 46 transcript and the recordings.

exhibit 41 table. First, of all, while exhibit 41 lists the offers received from 11 jewelers, there are only 10 encounters with jewelers in the exhibit 46 transcript, as there is a business card for “Gold Star Jewelers L.I., Inc.” for which there is no corresponding transcript in exhibit 46 or in the CD recording. Also, the exhibit 46 transcript for the encounters with Nice-N-Pretty Jewelry and Romanza does not demarcate where one ends and the next begins. Judging by the names given for the jeweler’s principal in the exhibit 46 transcript and comparing it with the business cards, it appears that the encounter starting on page 27 of the exhibit 46 transcript is with Nice-N-Pretty (and not Romanza Jewelry as shown in that transcript), while the encounter starting on page 28 with “Isaac” marks a new encounter, which is with Romanza Jewelry, whose business card lists “Isaac the Jeweler.”

24. Another problem is that, in a number of cases, the amounts offered for the jewelry match the amount written by Ms. Shnaider on the back of the business card for the jeweler in question, but that amount does not match the exhibit 46 transcript. Thus, Sean’s Fine Jewelry offered \$450.00 according to the exhibit 46 transcript, while the exhibit 41 table shows \$533.00, which matches the amount Ms. Shnaider recorded on the business card. Similarly, the offer from A+ Jewelry is \$430.00, according to the exhibit 46 transcript, but the exhibit 41 table lists an offer of \$460.00, which matches the amount Ms. Shnaider recorded on the back of that entity’s business card. The offer from Romeo & Juliet per the exhibit 46 transcript was \$520.00 and not the \$530.00 listed on exhibit 41, while the offer from Romanza per the exhibit 46 transcript was \$610.00 and not \$620.00, as shown on Romanza’s business card and the exhibit 41 table.

25. Correcting the exhibit 41 table for the above discrepancies and changing the title of the second column for accuracy yields the following table of the offers Ms. Shnaider received at Tri-

County:

Vendor Name	Highest Amount Offered <sup>6</sup>	Value of the Jewelry at Spot Value Gold Price ( <i>see</i> finding of fact 20).	% of Spot Value
Nice-N-Pretty	\$625	\$683.06	91.5%
Romanza	\$610	\$683.06	89.3%
Galeria Jewelry	\$540	\$683.06	78.4%
Baloochies	\$550	\$683.06	80.5%
Jewelers Pavillion	\$550	\$683.06	80.5%
Sean’s Fine Jewelry	\$450	\$683.06	65.9%
Romeo & Juliet	\$520	\$683.06	76.1%
Diamond King	\$508	\$683.06	74.4%
A+ Jewelry	\$430	\$683.06	63%
Jewelry by Akbash	\$450	\$683.06	65.9%
Gold Star Jewelers	\$450	\$683.06	65.9%

26. Ms. Shnaider testified that it is rare for consumers seeking to sell old gold to a jeweler to have a formal appraisal in hand because appraisals must be purchased. The exhibit 46 transcript of her interactions with the Tri-County jewelry vendors indicates that at least seven of the vendors knew that Ms. Shnaider was aware of the exact gold content of each item, usually because she would tell them the gold content (Nice-N-Pretty, Galeria Jewelry, A+Jewelry, Baloochies Design, Sean’s Fine Jewelry, Romeo and Juliet, and Jewelers Pavilion). She generally also made the jeweler aware that she was collecting offers from many booths and at

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<sup>6</sup> It is noted that at least four of the price estimates received were conditional in nature (*see* finding of fact 26).



five of the jeweler booths she exaggerated the price she had been offered for the jewelry (\$650.00). For example, at the next to last booth she visited, Romeo and Juliet, she stated that “[s]o far, I’ve been told around \$650,” when not a single jeweler had offered her that much. In at least four cases, the transcript makes clear that the amounts offered were given in an indefinite, non-binding fashion (“less than \$600, \$530 or something, \$550 something” [Galeria Jewelry], “I try and give you \$610” [Nice-N-Pretty], “I might give you” \$520 [Romeo and Juliet], “no more than \$450” [Jewelry by Akbash]). Two of the jewelers queried by Ms. Shnaider gave estimates based on their lower appraisals of the gold content of the six items of jewelry (Diamond King and Sean’s Fine Jewelry). Two others, in addition to giving cash offers, also gave store credit offers that were significantly higher (Jewelers Pavilion and Romeo & Juliet).

27. When Ms. Shnaider told him of receiving a \$650.00 offer, Galeria Jewelry’s sales person, Joseph, told her that “they just put you so higher that nobody can give that, can go back to them until they stop playing games with you.” Isaac of Romanza Jewelry warned her that jewelers at Tri-County would sometimes make a high offer and, when the customer came back to the booth, tell the customer that the offer was for the amount of credit she would get at the booth to buy jewelry there in return for the old gold. In the case of the prices offered by at least two of the jewelers, it is not clear whether the price is for cash or credit (Baloochies and Diamond King).

28. Mr. Ilyabayev testified that he writes checks for Milano, works with the company’s bookkeeper, and that he makes all the decisions for the company. According to Mr. Ilyabayev, a jeweler must have a license to buy old gold, must document the purchase in the police book, and must retain possession of the old gold for 15 days after purchasing it before disposing of it. He

testified that he gave customers 90% of the spot value of the old gold and that he sold most of the old gold he bought to Avital Gold Buyers, which pays him for the old gold based on the price in the London spot market on the day that he brings the gold to the refinery. He also testified that sometimes he gave store credit to customers in return for their old gold.

29. Mr. Ilyabayev asserted that, in addition to selling old gold to refineries, he also sold them new gold, which he referred to as “old stock,” and described as jewelry that was purchased from a wholesaler but which had been in his inventory for a while and “is no longer in fashion.” He claimed that Milano’s sales of old stock to the refineries were at a loss to the business because, in purchasing the jewelry Milano would have paid the wholesaler a markup of 20% to 25% above the spot market price of the gold in the jewelry and it would lose that markup when it sold the old stock to the refinery for its melt value. In reply to a question from his counsel whether Milano’s sales of old gold and old stock to refineries were “both substantial,” he answered affirmatively.

30. As further proof of the markup Milano paid for the gold jewelry it bought from wholesalers, petitioners introduced ten invoices for purchases of 14 karat gold jewelry items. Based on the weight of those jewelry items, and petitioners’ separate proof of the spot price of gold on the respective dates of those invoices derived from the Kitco.com website, petitioners showed that the markup Milano paid on those invoices above the spot value of the gold in those jewelry items varied from 1.04 to 1.32 times the spot price value of the gold therein, and averaged 1.20 times the spot price of the gold value. Mr. Ilyabayev testified that the invoices were representative of Milano’s purchases of jewelry during the audit period and the “prices paid relative to the value of gold and consistent with general business operations.”

31. Mr. Ilyabayev testified that on each page of the sales booklets given to the auditor he described the item being sold, along with the price and date, adding that he would also show the sales tax due. He testified further that during the years at issue his brother and two other employees also sold jewelry for Milano. He did not provide any testimony as to how the other employees of Milano prepared sales invoices, or even what instructions were given to them as to the information that should be noted on a sales invoice. He also did not describe what procedures, if any, Milano used to ensure that sales booklets were used in sequential order.

32. At hearing, petitioners produced an affidavit of Robert Kaykov, president of Avital Gold & Platinum, Inc. (Avital), notarized on May 12, 2015. In the affidavit, Mr. Kaykov asserts that he has been doing business with Mr. Ilyabayev for five years and during that time has purchased large amounts of gold from Milano on a frequent basis. During that time, he paid 98.75% of the daily price of gold based upon the London Fixed Price. According to the affidavit,

“5. Much of the merchandise I purchase from Milano consists of out of date or out of style new merchandise.”

6. I know, for a fact, that much of the merchandise I purchase from Milano is new by the fact so much of this merchandise consists of similar and duplicated pieces.

7. I also know, from my personal examination of the Milano jewelry, that the majority of the inventory is new, outdated and out of style.”

Mr. Ilyabayev testified that he personally took the affidavit to Mr. Kaykov for his signature, but that he did not remember who drafted the affidavit.

33. Based on their contentions that the auditor should have used 85% as the average payout percentage of jewelers and that Milano lost 22.5% on its sale of new gold to the refineries, petitioners' hearing brief presents a computation showing that Milano only slightly

under-reported the sales tax it owed on its sales tax returns. More specifically, using the 85% as the average payout percentage of jewelers and the 95% refineries' average payout percentage applied by the auditor, petitioners calculate that Milano's sales of old gold to the refineries could have only accounted for \$1,577,076.00 of the total of Milano's sales to the refineries ( $\$1,411,068.00 \div .85 \times .95$ ). Petitioners then assume that the difference between this amount and Milano's total receipts from the refineries, \$1,531,876.14 ( $\$3,108,952.14 - \$1,577,076.00$ ), must have come from Milano's sales of new gold to the refineries. Petitioners next compute the cost of that amount of new gold to Milano by dividing the \$1,531,876.14 figure by 95% to reflect the 95% refineries' average payout percentage and multiplying it by 122.5% to reflect the average markup Milano pays to wholesalers relative to the spot value of the gold in the jewelry (citing its hearing proof summarized in finding of fact 30), which equals \$1,975,313.97. Subtracting both Milano's cost for the new gold sold to the refiners (\$1,975,313.97) and its cost of the old gold sold to the refiners (\$1,411,068.00) from its total purchases (\$4,142,961.31) yields gold jewelry purchases available for sale to its retail customers of \$756,579.34 ( $\$2,731,893.31$  less \$1,975,313.97). Marking up that amount of gold purchases by Milano's 49.97% retail markup percentage found on audit yields audited sales of \$1,134,642.04, which is only \$2,477.04 more than the sales reported by Milano on its sales tax returns (\$1,132,165.00).

34. The price of gold fluctuates daily. The April 2013 post on the New York Times blog *Economix* (*see* finding of fact 20) notes that "the price of gold roughly doubled between 2009 and 2011," after which, "the price has fallen fairly steadily, reaching about \$1,600 an ounce before a sharp break in the last two weeks that brought the price down to \$1,400 an ounce."

***POSITIONS OF THE PARTIES***

35. Petitioners argue that the notices of determination issued to them should be cancelled because they were based on the Division's performance of an estimated audit without proper justification. According to petitioners, it was improper for the Division to perform an estimated audit here because (i) the Division did not make a proper request for records, as the Division failed to request Milano's POS system sales records, (ii) the Division only reviewed Milano's sales records for a single quarter, and (iii) the books and records Milano supplied on audit were an adequate basis on which to perform an audit in any case. Petitioners also argue that the Division's audit method of estimating sales tax due in this matter was not reasonably calculated to reflect the taxes due because it applied Milano's markup on retail sales to all of Milano's purchases of new gold, notwithstanding that the auditor knew that some of Milano's purchases of new gold were sold at a loss to refineries. Finally, petitioners argue that, even assuming the additional sales tax found due on audit is upheld, penalty should be abated because there existed reasonable cause and a lack of willful neglect for the additional tax found due.

36. The Division maintains that the notices issued to petitioners should be sustained in full. It claims that the auditor made an adequate request for Milano's books and records, thoroughly reviewed them for all of the quarters of the audit period, and properly concluded that they were inadequate for audit because the sales records were not in auditable condition. It further argues that petitioners have failed to show reasonable cause and the lack of willful neglect for the additional tax found due on audit and that, therefore, the penalty portion of the assessments should be sustained.

**CONCLUSIONS OF LAW**

A. Tax Law § 1138 (a) (1) provides, in relevant part, that if a sales tax return was not filed, “or if a return when filed [was] incorrect or insufficient, the amount of tax due shall be determined by the [Division of Taxation] from such information as may be available. If necessary, the tax may be estimated on the basis of external indices . . . .” Case law establishes that the Division must satisfy a few requirements before it may resort to its authority under Tax Law § 1138 (a) (1) to estimate a vendor’s liability based on external indices. First, it must make a request for the vendor’s books and records that is more than “weak and casual” (*Matter of Christ Cella, Inc. v State Tax Comm'n*, 102 AD2d 352, 354 [3d Dept 1984]). Then, it must thoroughly examine the books and records for the entire period of the proposed assessment to determine if they are an adequate basis on which to perform an audit (*see Christ Cella; Matter of King Crab Rest. v Chu*, 134 AD2d 51 [3d Dept 1987]; *Matter of Adamides v Chu*, 134 AD2d 776 [3d Dept 1987], *lv denied* 71 NY2d 806 [1988]). The Division may not use such external indices unless it determines, after such an examination of the vendor’s records, that “it is virtually impossible to verify taxable sales receipts and conduct a complete audit with available records” (*Christ Cella*, 102 AD2d at 353), “from which the exact amount of tax due can be determined” (*Matter of Mohawk Airlines v Tully*, 75 AD2d 249, 251 [3d Dept 1980]). Tax Law § 1135 mandates that “[e]very person required to collect tax shall keep records of every sale ... and of all amounts paid, charged or due thereon and of the tax payable thereon, in such form as the commissioner of taxation and finance may by regulation require . . . .” The regulations provide that among the sales records required to be maintained are each “sales slip, invoice, receipt, contract, statement, or other memorandum of sale” (20 NYCRR 533.2 [b] [1]). The sales

records must provide sufficient detail to independently determine the taxable status of each sale and the amount of tax due and collected thereon unless such information may be obtained from the vendor's other records (*see* 20 NYCRR 533.2 [b] [2]).

B. Petitioners first argue that the auditor did not make an adequate request for Milano's books and records because the only written record request did not ask for Milano's POS records. Petitioners claim that the auditor knew from her pre-audit inspection of Milano's booths that it had a POS system. The auditor's initial letter to Milano's representative at the time, Mr. Izyayev, included an IDR that asked for all of Milano's "sales invoices" (*see* finding of fact 4). The auditor testified that a POS system maintains electronic records of a sale in a database and can generate an invoice for the sale at any time. The reasonable intendment of the term "sales invoices" includes invoices that can be generated using a POS system, especially when the attached audit appointment letter instructed Milano to provide "any and all documentation in auditable form and electronic form (if available) which supports the sales and use returns as filed" (*see Matter of DeFilippis*, Tax Appeals Tribunal, June 9, 1994 [finding that a request for "(a)ll books and records pertaining to sales tax liability" satisfied the *Christ Cella* more than "weak and casual" standard]). Accordingly, petitioners' argument is rejected.

C. Petitioners next argue that the books and records Milano produced on audit were an adequate basis for the audit and that, in reaching the opposite conclusion, the auditor failed to conduct a thorough inspection of those books and records for each quarter of the audit period, as she was required to do. The Division's auditor testified that Milano's sales records were not maintained in a manner that would permit a complete audit to be performed on them. Specifically, she testified that the sales booklets, which Milano used to record sales, were not in

sequential order and that the individual sales slips did not include adequate descriptions of what was being sold, were not dated properly, sometimes did not have sales totals properly added, and did not even include Milano's name on them. Some of these alleged problems with Milano's sales records, however, do not appear to be of sufficient gravity to make it impossible for the auditor to determine whether Milano owed additional sales tax. This is true with regard to the complaint that the sales slips' individual charges may not have been added, especially given the lack of testimony that the problem was pervasive enough to effectively prevent the auditor from determining if proper sales tax had been charged. Similarly, the failure of the sales slips to properly describe the item being bought also does not appear sufficient to prevent a determination if the invoice is taxable since, as a seller of jewelry, Milano was not claiming any use-based exempt sales and apparently did not claim any nontaxable sales at all, other than sales for resale, at least during the test period of March 1, 2013 through May 31, 2013.

D. Milano's failure to use sales slips in sequential order, however, is sufficient to preclude a determination whether Milano had collected and remitted proper amount of sales tax because it prevented the auditor from knowing whether she had all of Milano's invoices for the audit period (*see Matter of Mediabuss Sys., Inc.*, Tax Appeals Tribunal, March 18, 2014 [finding that the lack of any prenumbering or sequential numbering on the invoices themselves, as well as the lack of any cash receipts journal, general ledger, trial balances, or other summary schedules, demonstrates a lack of internal control over the invoices and precludes the possibility of verifying the completeness of the sales invoices that were made available]; *see also Matter of Aum SidhdyVinak, LLC*, Tax Appeals Tribunal, December 8, 2011). While petitioners produced evidence at hearing, through the testimony of Mr. Ilyabayev, disputing the existence of the other



deficiencies in the sales records cited by the auditor, Mr. Ilyabayev did not testify as to what internal controls, if any, Milano had in place over the invoices used by Mr. Ilyabayev and Milano's three other employees. Alternatively, petitioners could have produced Milano's sales slips at hearing to show that Milano did use the sales booklets in sequential order. Petitioners also did not do this. Thus, petitioners failed to meet their burden of proof of showing that Milano maintained adequate records that the auditor simply disregarded.

E. Petitioners next argue that the auditor only reviewed Milano's sales records for a single quarter, in violation of the rule from *Adamides* that the adequacy of the records must be determined on a quarter by quarter basis. Quite to the contrary, the auditor testified that she reviewed all of the sales records that were provided at Mr. Izyayev's office. She further testified that she sorted the sales booklets by quarter and then chose the quarter with the most sequential sales books to review in detail, the March 1, 2013 through May 31, 2013 quarter. Her testimony is consistent with the audit log entry for November 8, 2013, which refers to the deficiencies in the sales booklets and states that "on review" a quarter was chosen for in-depth analysis. Accordingly, petitioners' argument that the auditor did not review Milano's records on a quarter by quarter basis is rejected.

F. Petitioners point out that, under the Division's sales tax field audit guidelines, the auditor was required to note any contact of relevance to the audit, yet here the audit file lacks documentation of many crucial aspects of the audit. In this regard, petitioners point to the fact that the auditor did not document the inadequacy of Milano's records, as she did not retain copies of the defective sales slips and did not make notes of the invoice sequences used by Milano except for the tested quarter. According to petitioners, this leaves the audit file "legally

insufficient to support a deficiency” and entitles petitioners to an inference that the “withheld evidence” would not be favorable to the Division, citing *Sarach v M&T Bank Corp.*, 140 AD3d 1721 [4<sup>th</sup> Dept 2016]). These arguments are unavailing. First, as discussed in conclusion of law E, petitioners' argument to the contrary, the audit log here indicates that the auditor did not limit her review of Milano's sales records to the tested quarter. More broadly, while auditors are well advised to maintain audit files that thoroughly document the audit they performed in order to avoid proof issues at hearing, the failure to do so does not preclude the Division from proving what happened on audit through other means. For instance, in *Matter of Majestic Deli Grocery, Inc.* (Tax Appeals Tribunal, April 14, 2017), the petitioners contended that the auditor did not properly review the vendor's purchase records on audit, citing the fact that the auditor did not transcribe all of the invoices that she reviewed at the time of the field audit appointment at issue. The Tribunal rejected the argument, reasoning “[s]uch indirect evidence is insufficient to establish petitioners' factual claim, given the auditor's credible testimony and the tax field audit record entries, as noted, and the lack of any other evidence in the record supporting petitioners' claim.” Here, too, the auditor supplied credible testimony that she reviewed all of Milano's sales records, which testimony is buttressed by the audit log, and there is no evidence contradicting that testimony. Finally, it bears noting that if, contrary to the auditor's testimony, Milano did maintain proper sales records, petitioners should have produced those records at hearing, which they did not do here.

The undersigned found the auditor's testimony to be credible, including her testimony about her examination of Milano's books and records. Against this conclusion, petitioners cite mainly the statement in the audit report that the tax found due on audit was calculated using

Milano's own records and not internet sources (*see* finding of fact 8). Petitioners contend that statement is contradicted by the audit file, which makes clear that the auditor relied on internet resources in determining the average payout percentage of jewelers for purposes of her confirmation test. With this argument, petitioners conflate the auditor's method of calculating the tax found due on audit, which was a markup test using Milano's own books and records, with the confirmation test the auditor used to analyze petitioners' assertion that Milano's sales of old gold to refineries were not sufficient to explain the amount of its receipts from those refineries, in which the auditor did rely on information from the internet (*see* findings of fact 8, 11).

Accordingly, this argument does not undermine the auditor's credibility.

G. The next issue is whether the method the Division used to estimate Milano's liability here was reasonably calculated to reflect tax due. The Division calculated the tax due by accepting Milano's figure for total purchases of jewelry from its general ledger, subtracting out its purchases of old gold from that total, to arrive at Milano's purchases of gold jewelry for retail sale, and applying a 49.97% markup to that amount. The markup percentage was derived from Milano's own records (*see* finding of fact 8). Estimating a vendor's liability by means of a markup of its purchases has been determined to be a reasonable method for reflecting the tax due from the vendor (*see e.g. Matter of Ahmed*, Tax Appeals Tribunal, April 14, 2011). Thus, the burden is on petitioners to show that "the result of the audit was unreasonably inaccurate or that the amount of tax assessed was erroneous" (*id.*, citing *Matter of Sarantopoulos v Tax Appeals Trib.*, 186 AD2d 878 [3d Dept 1992]). This is "a fairly substantial burden" (*Matter of Ahmed*). Crucially, the determination of whether the method chosen by the Division was reasonable is based on the information available to the Division at the time of the issuance of the notice (*see*

*Matter of Cont. Arms Corp. v State Tax Commn.*, 72 NY2d 976 [1988]).

Petitioners argue that the audit result here is unreasonable because the audit fails to take into account that some of the new gold that Milano purchased was sold for its melt value to refineries. According to petitioners, when Milano sold new gold to the refineries, it did so at an average loss of 25%. Thus, in petitioners' view, by refusing to take into account these sales of new gold to the refineries, the auditor applied a 49.97% markup to a sale that actually occurred at a loss to Milano. As proof that some of the new gold purchased by Milano was sold to refineries, petitioners point to: (1) the statements that Milano's representative, Mr. Ilyayev, made to the auditor that Milano's sales to the refineries included substantial amounts of new gold; (2) the affidavit from Mr. Kaykov, Avital's president, that Milano often sold it new gold; and (3) the auditor's confirmation test, which, petitioners claim, if properly done, would have shown that the sales of old gold could not have explained, by themselves, the amount of the receipts that Milano earned from the refineries.

The Kaykov affidavit relied on by petitioners is dated May 12, 2015 (finding of fact 32), which is after the December 8, 2014 issuance date of the notice herein. Accordingly, it may not be relied upon as a basis for undermining the reasonableness of the audit (*see Cont. Arms Corp.*). As for the statements made by petitioners' prior representative that some of the sales to the refineries consisted of new gold, those statements, unsupported by any source documentation, are not sufficient to require the auditor to assume that Milano was selling new gold to the refinery (*see Matter of Robritt Liquor Store, Inc.*, Tax Appeals Tribunal, December 27, 1991 [testimony by taxpayer's witness that the assistant auditor would not have time to have written down all of the taxpayer's prices that were used on the audit was found not to be sufficient to render the audit

unreasonable when the taxpayer failed to actually prove the prices used by the auditor were wrong]). Moreover, the auditor, in the audit log, paraphrases Mr. Izyayev, Milano's representative at the time of the audit, as claiming that the sales of new gold to the refineries occurred at the end of the year, yet the auditor's transcription of Milano's receipts from the refineries for two of the audit years does not show any consistent, significant spike of sales at the end of the year or the beginning of the next and petitioners provided no explanation (*see* finding of fact 10).

H. As a basis for undermining the rationality of the audit, that leaves petitioners' contention that the auditor's confirmation test, if properly done, would have revealed that Milano's sales to the refineries included new gold, presumably requiring application of a different markup percentage to purchases of the new gold sold to refineries, instead of at retail. According to petitioners, that test would have revealed that some of Milano's sales to the refineries must have been new gold if the auditor had used a correct jewelers' average payout percentage. Petitioners maintain that the auditor "backed into" the 40% jewelers' average payout percentage she used in her test and claimed to have derived from her internet research, i.e., that the 40% jewelers' average payout percentage "was a contrivance" to avoid the conclusion that Milano's sales to the refineries must have included new gold. To demonstrate that the auditor failed to make a good faith effort to identify the correct jewelers' average payout percentage, petitioners point to the fact that, of the seven "internet resources" excerpted in the audit file to support the 40% jewelers' average payout percentage, only two address the issue and those two are not credible. Petitioners make the further claim that Ms. Shnaider's testimony shows that there were internet resources available to the auditor that would have steered her to the correct

jewelers' average payout percentage.

To show the importance of the issue of the use of a proper jewelers' average payout percentage, petitioners point out that if the auditor had used any figure higher than 43.1% for the jewelers' average payout percentage, the auditor would have realized that the old gold could not explain all of Milano's receipts from the refineries.<sup>7</sup> Instead of 40%, petitioners urge that 85% is the correct figure for the average payout percentage of jewelers, which is the payout percentage cited by the Consumer Reports website, and is consistent, petitioners claim, with the average payout percentage ranges cited by the other articles found by Ms. Shnaider through her internet research (*see* finding of fact 17). In their hearing brief, petitioners present a calculation that if the 85% jewelers' average payout percentage is used, and the further assumption is made that Milano loses 22.5% on its sales of new gold to the refineries, it follows that Milano under-reported its sales tax liability for the audit period by only \$2,477.04 (*see* finding of fact 32).

For the reasons discussed below, it is determined that the auditor did not have a basis for adjusting the audit liability on the theory that some of Milano's purchases were of new gold sold to refineries at a loss and that the auditor's confirmation test, even as revised by petitioners, could not have provided such a basis.

I. The Tribunal has stated that "[w]hile it is advisable to do so, auditors are not required by law to confirm the reasonableness of the results of their chosen methodology" (*Matter of 33 Virginia Place, Inc.*, Tax Appeals Tribunal, December 23, 2009). Here, even if the confirmation test was an adequate means of showing that some of Milano's purchases of new gold must have

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<sup>7</sup> The 43.1% figure is derived by dividing \$1,411,068.00 (the amount Milano paid for the old gold) by \$3,272,581.20 (the amount of Milano's receipts from the refineries [\$3,108,952.14] divided by 95% to reflect the average payout percentage of refineries).

been sold to refineries, which, as discussed below, it was not, the auditor would still not have been required to make an adjustment to her markup estimation methodology because Milano failed on audit (as at hearing) to show that it had actually sold new gold to the refineries and failed to provide source documentation identifying such sales (*see Robritt Liquor Store, Inc.; On the Rox Liquors, Ltd. v State Tax Commn.*, 124 AD2d 402 [3d Dept 1986], *lv denied* 69 NY2d 603 [1987] [notwithstanding that petitioner kept a file of facially valid exemption certificates, because petitioner could not tie those certificates to a particular sale, petitioner was not entitled to a further adjustment excluding some sales as sales to exempt organizations]; *Matter of Reference Lib. Guild*, Tax Appeals Tribunal, August 4, 1988 [Tribunal is “persuaded” that petitioner has out-of-state sales, but it upheld an audit as reasonable that treated all of petitioner’s sales as taxable because of petitioner’s inability to prove any particular sale was out-of-state]).

J. In any event, petitioners’ version of the confirmation test, with a higher jewelers’ average payout percentage, does not constitute clear and convincing proof that Milano made sales of new gold to the refineries. One problem is that petitioners’ version merely repeats a flaw in the auditor’s confirmation test. Whether the \$1,411,068.00 of Milano’s old gold sales could have led to \$3,108,952.14 in receipts from the refineries depends on what markup Milano achieved on its sales of old gold, i.e., the difference between what it pays for the old gold and what it receives for the old gold. The auditor focused on the average payout percentage of jewelers – the jeweler’s markup relative to the spot value of gold on the day of the purchase from the consumer, which she determined to be 40% – and then compared it to the average payout percentage of refineries – the percentage of the spot value that jeweler received from the refinery when it sold the old gold to the refinery, which she determined to be 95%. The difference

between these two percentages, however, is not a good surrogate for a jeweler's actual markup on old gold sold to a refinery, because the jeweler must hold the jewelry for two weeks before selling it to the refinery. In that two week gap, the price of gold could have changed, as the price of gold changes daily (*see* finding of fact 33). To the extent that the price of gold increased within the two weeks a jeweler was required by law to hold the gold, its markup on the gold would have gone up. Use of a jewelers' average payout percentage to determine Milano's actual markup percentage completely overlooks this problem and petitioners' substitution of a 85% jewelers' average payout percentage for the auditor's 40% jewelers' average payout percentage just continues this flaw in the auditor's confirmation test. Given that gold apparently doubled in value between 2009 and 2011 (*see* finding of fact 33), this flaw materially detracts from the reliability of petitioners' revised version of the confirmation test.<sup>8</sup>

Furthermore, even assuming that the difference between the average payout percentage of jewelers and the average payout percentage of refineries is an adequate surrogate for the relevant markup factor, petitioners' proof that the auditor's use of a 40% jewelers' average payout percentage is significantly wrong is not persuasive. That proof consists of petitioners' critique of the internet sources cited by the auditor in support of her 40% jewelers' average payout percentage, the internet sources found by Ms. Shnaider, and the Tri-County investigation.

K. It is true, as petitioners contend, that the two websites used by the auditor as a basis for

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<sup>8</sup> This problem is also relevant to petitioners' claim that Milano experienced an average loss of 20% to 25% on its claimed purchases of new gold to the refineries (*see* findings of fact 29 and 30), based on their proof that Milano pays 20% to 25% above the spot value of the gold in the gold jewelry it buys from wholesalers on account of the workmanship that goes into the jewelry. But petitioners' proof does not consider the possibility that the spot price of gold may have increased since Milano purchased the new gold jewelry, in which case Milano might have lost less than 20% to 25%, or not have lost money at all, when it sold that new gold to refineries. Because petitioners have not traced a purchase of new gold jewelry through to its sale to a refinery, petitioners have not proven that Milano lost an average of 20% to 25% on the sale of any new gold it sold to refineries.



the average payout percentage of jewelers do not provide an adequate basis for the auditor's use of a 40% figure. One, the American Gold Refinery site, notes no author, and does not even specify a jewelers' average payout percentage, stating merely that jewelers, pawn shops or on-line gold buyers "pay 30-50% less than a reputable and trusted gold refinery," without providing any basis for the source of that knowledge. Its chief purpose appears to be to attract sellers of old gold to itself, and away from other gold jewelry buyers. The second website used by the auditor, [www.make-money-gold.com](http://www.make-money-gold.com), provides no basis for its statements that "legitimate dealers" pay between 40% and 65% of the value of the old gold's gold content or that paying 50% of the value of the gold in the old gold is what "most legitimate gold dealers" pay.

The articles cited by petitioners, however, are also not persuasive proof of the correct jewelers average payout percentage (*see* finding of fact 17). Petitioners rely chiefly on the Consumer Reports article, which, while giving no author, and citing no sources, offers the single sentence, "Aim to get about 85 percent of what you calculated it's worth." Given that the article does not even claim that Consumer Reports researched the issue, it cannot be accorded much evidentiary weight (*see Matter of Fashana*, Tax Appeals Tribunal, September 21, 1989 [Tribunal finds that statistical charts for various industries, which were purportedly derived from Federal income tax returns but did not reveal the authorship or methods by which the charts were created, did not constitute a rational basis for a sales tax estimated audit]). The remaining articles cited by petitioners are similarly flawed, as all are written in terms of what percent of the gold jewelry's true value a consumer might "expect" to get and none cites any authority for the percentage given (*see* finding of fact 17). In short, the articles do not constitute clear and convincing proof of the appropriate jewelers' average payout percentage.

L. For a number of reasons, the Tri-County investigation also does not provide clear and convincing proof of what markup Milano realized on its sales of old gold. First, Ms. Shnaider only got offers from 11 of the 19 booths at Tri-County that sold gold and her testimony was not clear in why should did not get offers from the remainder (*see* finding of fact 21). Second, it is far from clear that Ms. Shnaider, who had worked in a jewelry store and had sold old gold before, was a typical old gold seller. In regard to seven of the jewelers, she made known the gold content of the six items of jewelry. This is important because it might have caused some of the jewelers to opt not to use their presumably superior knowledge of gold content to give a “lowball” offer by deceiving her about the gold content of the jewelry, which two of the jewelers did anyway. Petitioners did not establish that such knowledge is typical of consumers seeking to sell old gold; if anything, the record gives some reason to doubt that it is typical because Ms. Shnaider testified that it is rare for consumers to get formal appraisals because they cost money. Third, four of the offers were conditional in nature, e.g., “less than \$600” (finding of fact 26), so it is not clear that the amount listed in the table in finding of fact 25 would have been realized by Ms. Shnaider, had she actually attempted to consummate the transaction. Two different vendors warned her of the presence of jewelers at Tri-County who might make inflated offers in the hope of luring her back to them and negotiating a lower offer when she returned. Lastly, the table in finding of fact 25 fails to take into account that at least two of the jewelers made her “store credit” offers, i.e., offers in which she could get a higher “store credit” amount than the “cash” amount that they could otherwise offer her. Presumably, they could offer higher store credit amounts because of the markups built into the prices of their stores’ inventory. Given the vendors’ willingness to make these higher store credit offers, such store credit deals are

presumably more profitable. Mr. Ilyabayev testified that Milano also gave such “store credit” deals, meaning Milano also enjoyed the higher markup of such transactions. By ignoring all such offers, and only listing the lower markup “cash” offers, the Tri-County investigation is not persuasive proof that the auditor should have used an 85% jewelers’ average payout percentage as petitioners urge.

M. At most the internet sources and the Tri-County investigation indicate that the 40% jewelers’ average payout percentage used by the auditor was arguably too low for a jeweler operating at Tri-County, but that proof falls far short of establishing the correct amount of the average payout percentage of jewelers at that venue. Thus, even if the confirmation test is an appropriate way of testing whether Milano’s sales to the refineries included some new gold, petitioners did not prove *how much* of Milano’s receipts from the refineries was from new gold, making it impossible to know whether applying the 49% markup to all of Milano’s purchases from wholesalers, without excluding any as sold at a lower markup as new gold to the refineries, caused the audit to be unreasonably inaccurate (*see Matter of Pizza Works, Inc.*, Tax Appeals Tribunal, March 21, 1991 [“Since petitioner's failure to maintain records prevents exactness, exactness in determining the sales tax liability is not required,” citing *Matter of Meyers v. State Tax Commn.*, 61 AD2d 223 (3d Dept 1978), *lv. denied* 44 NY2d 645 (1978)]).

N. The Division asserted penalty herein pursuant to Tax Law § 1145 (a) (1) (vi). Tax Law § 1145 (a) (1) (vi) provides that any person who omits 25% or more of the total amount of tax required to be shown on a sales tax return “shall be subject to a penalty equal to ten percent of the amount of such omission.” Penalties imposed under section 1145 (a) (1) (vi) must be sustained unless a petitioner can show the failure was due to reasonable cause and not due to

willful neglect. In establishing reasonable cause for penalty abatement, the taxpayer faces an onerous task (*Matter of Philip Morris, Inc.*, Tax Appeals Tribunal, April 29, 1993). Petitioners' only argument for penalty abatement is that they properly complied with the Tax Law and did not owe the tax liability found due on audit. Because that assertion is rejected above, petitioners' request for penalty abatement is also rejected.

O. Mr. Ilyabayev also challenges his status as a person required to collect tax on behalf of Milano (*see* Tax Law §§ 1131 [1]; 1133 [a]; 1138 [a] [3] [B]). While petitioners' representative at hearing stated that petitioners were still pursuing that issue, Mr. Ilyabayev did not submit any arguments in support of this position in their hearing brief. In any event, because Mr. Ilyabayev was president and sole owner of Milano, and the person who made all decisions for Milano (*see* findings of fact 1 and 28), the Division properly treated him a person required to collect tax on behalf of Milano.<sup>9</sup>

P. The petitions of Milano and Son, Inc. and Iosif Ilyabayev are denied and the notices of determination, dated December 8, 2014 and December 9, 2014, respectively, are sustained.

DATED: Albany, New York  
December 27, 2018

/s/ James P. Connolly  
ADMINISTRATIVE LAW JUDGE

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<sup>9</sup> The petitions herein also raise a number of issues that petitioners did not address at hearing or in their hearing brief. Those issues are therefore deemed abandoned.