

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition :  
of :  
**BIG STAR NUNEZ CORPORATION** : DETERMINATION  
for Revision of a Determination or for Refund of Sales and : DTA NO. 827572  
Use Taxes under Articles 28 and 29 of the Tax Law for the :  
Period September 1, 2009 through May 31, 2012. :

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Petitioner, Big Star Nunez 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 September 1, 2009 through May 31, 2012.

A hearing was held before Donna M. Gardiner, Administrative Law Judge, in New York, New York, on December 5, 2017 at 11:00 a.m., with all briefs to be submitted by March 26, 2018, which date began the six-month period for the issuance of this determination. Petitioner appeared by Eddy Estrella, CPA. The Division of Taxation appeared by Amanda Hiller, Esq. (Osborne K. Jack, Esq., of counsel).

***ISSUES***

I. Whether the Division of Taxation properly issued a notice of determination assessing sales and use taxes due for the period September 1, 2009 through May 31, 2012.

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

***FINDINGS OF FACT***

1. Petitioner, Big Star Nunez Corporation, owned and operated a deli at 1180 Sunrise Highway, Copiague, New York during the period September 1, 2009 through May 31, 2012 (audit period).

2. On July 13, 2012, the Division of Taxation (Division) began an audit of petitioner's sales and use taxes for the audit period. The auditor sent to petitioner an audit appointment letter, dated July 16, 2012, that included an information document request (IDR) in order to perform the audit. The records requested included: sales tax returns, worksheets and canceled checks, federal income tax returns, general ledger, sales invoices, exemption documents, bank statements with canceled checks and deposit slips, cash receipts journal and cash disbursement journal. A second request for documents was made by letter dated August 2, 2012.

3. On October 15, 2012, the Division conducted a field audit appointment with petitioner's then representative. The Division received bank statements, but petitioner did not provide any register tapes or sales invoices to substantiate the amounts on the bank statements. The Division requested, but did not receive any canceled checks or any documentation that showed purchases made by the business. Therefore, the auditor concluded that the taxpayer's records were inadequate to allow the Division to determine if the deli had reported the proper amount of tax due. The Division chose to conduct an observation of the deli to determine if petitioner owed any additional tax.

4. On October 18, 2012, the auditor reviewed the business' purchase records. The auditor noted that for 2009, petitioner's purchases, reflected by its own invoices, exceeded sales reported for the same period. The auditor asked petitioner's former representative to prepare a schedule of

petitioner's monthly purchases for the period in issue. Petitioner denied this request and asked the auditor to contact its suppliers directly to obtain purchase information.

5. On October 19, 2012, petitioner objected to the Division's choice to perform an observation test of the business. Petitioner requested that the auditor use a different method to compute its tax liability. The Division informed petitioner that if the auditor was denied access to entering the deli to conduct the observation, then the Division would conduct the observation from outside the premises by counting the number of patrons and use an average price to determine sales.

6. On December 7, 2012, the Division attempted to conduct an observation of petitioner's business activities. The Division was prevented from entering the business. Therefore, the Division conducted an observation from outside the business from 5:00 a.m. to 10:10 p.m. Although the auditor was told that the business hours of operation were 5:00 a.m. to 11:00 p.m., on the date of the observation test, the business closed at 10:10 p.m.

7. At the conclusion of the observation, the Division requested copies of the day's register tapes but was told that the business did not have register tapes. The Division then observed an employee count \$2,700.00 in receipts for the day. The auditor used the \$2,700.00 in receipts for the day and applied that number over the audit period. This resulted in additional tax due in the amount of \$223,197.01 plus penalty and interest. The auditor issued a statement of proposed audit changes to petitioner in this amount.

8. At this point, the audit file was transferred to another auditor. It was discovered that the additional tax due asserted in the statement of proposed audit changes was in error. The auditor found that the additional tax due was overstated because the Division did not subtract sales tax

included in the amount of \$2,700.00 before applying that number to the entire audit period. After subtracting the tax paid, the amount in additional tax due was \$189,868.35.

9. In response to the statement of proposed audit changes, petitioner alleged that the receipts for the observation day included lottery sales and Western Union money transfers. Petitioner claims that only \$1,000.00 reflected actual sales for the day. However, petitioner did not provide any documentation to substantiate lottery sales or Western Union money transfers. The Division then decided to use petitioner's purchases to conduct the audit.

10. The Division sent letters to petitioner's suppliers to verify purchases. All but four suppliers responded. Based upon the responses received, the Division determined that petitioner had made at least \$1,183,299.86 in purchases during the audit period. The invoices provided by petitioner for the same period, for the same vendors, reflected only \$272,686.05 in purchases.

11. To compute purchases from the vendors that did not respond to the Division's letter, the auditor divided total verified purchases, in the amount of \$1,183,299.86, by total purchases as reflected by the invoices that petitioner supplied, in the amount of \$272,686.05, that resulted in an error rate of 4.33. The auditor then totaled the invoices for the non-responsive vendors, i.e., Daily Bread Distributors, Inc. - \$7,579.96, Derle Farms - \$5,550.06, Essex House Coffee Company, Inc. - \$1,921.89, and Leo's Products - \$22,074.00, to determine total unverified purchases from these vendors in the amount of \$37,125.91. This amount of unverified purchases was multiplied by the error rate of 4.33 to determine audited purchases from these four vendors in the amount of \$161,104.99. This amount of \$161,104.99 was then added to the total verified purchases in the amount of \$1,183,299.86 to determine total purchases for the audit period in the amount of \$1,344,404.85.

12. The auditor then used a cost of goods sold factor from the Almanac of Business and Industrial Financial Ratios (Almanac), 2012 Edition, to determine petitioner's sales for the period in issue. The Almanac provided financial ratios based on data collected from actual Federal returns filed by businesses. The information provided in the Almanac is grouped by the North American Industry Classification System (NAICS) coding system. The NAICS groups businesses with similar characteristics together so that, for example, information on retailers is provided separate from information on wholesalers.

13. On petitioner's United States income tax returns, the NAICS code is referred to as "Business Activity Code Number." On its returns for the tax years 2010, 2011 and 2012, petitioner selected code 445110. After reviewing the codes in the Almanac and comparing them to the code shown on petitioner's filed income tax returns, the auditor determined that there were no codes in the Almanac that directly corresponded to the one listed on petitioner's tax returns. The auditor then determined that the code for food and beverage stores, i.e., 445115, was most applicable to petitioner's business.

14. Within the Food and Beverage Stores sector, the Almanac presented ratios for cost of operations relative to sales. It lists different cost of operations percentages for the businesses surveyed, based on the dollar value of assets reported on such business' tax returns. Thus, the cost of operation percentage was different for businesses with: zero assets, assets under \$500,000.00, assets between \$500,000.00 and \$1 million, and continued to a maximum for businesses with assets in excess of \$2.5 billion.

15. Petitioner reported zero assets on each of its tax returns for the years 2010, 2011 and 2012. Based upon this fact, the auditor selected the percentage for a cost of operations factor for businesses with zero assets, i.e. 63%. This cost of operations factor was applied to audited

purchases in the amount of \$1,344,404.85 to determine audited gross sales in the amount of \$2,133,975.95. Of this amount, the auditor applied a taxable percentage of 90% that reflected taxable sales in the amount of \$1,920,578.36.<sup>1</sup>

A 90% taxable sales percentage was estimated by the Division based upon the fact that petitioner provided no documentation from which a taxable ratio could be determined. Additionally, as noted in finding of fact 6, petitioner refused access to its business in order for the Division to conduct an observation of sales. The estimated taxable ratio was determined by a survey of the deli, the overall size of the deli and the portion of the deli dedicated to selling taxable goods.

16. Once the auditor determined taxable sales in the amount of \$1,920,578.36, the auditor credited petitioner for taxable sales reported on its returns in the amount of \$280,613.00 to determine the amount of additional taxable sales of \$1,639,965.36 and additional tax due for the period in issue in the amount of \$141,447.01.

17. At the conclusion of the audit, the Division issued a notice of determination, assessment number L-042694801, dated April 10, 2015, to petitioner asserting additional tax due of \$141,447.01, plus penalties and interest.

18. The Division presented the testimony of its auditor at the hearing. The auditor described the request for books and records, the insufficiency of the books and records presented and details regarding the audit methodology employed.

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<sup>1</sup>It is noted that applying a 63% cost of operations factor to audited purchases in the amount of \$1,344,404.85 results in a larger amount than that used by the auditor herein. Such error was continued through the application of the taxable sales percentage, which error inured to the benefit of petitioner. Therefore, the lower amounts used by the Division shall not be corrected by this determination.

19. Petitioner did not dispute that it presented inadequate books and records from which a detailed audit could be performed. Petitioner did not present any witnesses or submit any documents to challenge the Division's audit in this case.

### ***CONCLUSIONS OF LAW***

A. Pursuant to Tax Law § 1132 (c) (1), petitioner bore the burden of proving by clear and convincing evidence that the tax assessed was erroneous (*Matter of Rizzo v Tax Appeals Trib. of State of N.Y.*, 210 AD2d 748 [3d Dept 1994]; *Matter of Mobley v Tax Appeals Trib. of State of N.Y.*, 177 AD2d 797 [3d Dept 1991], *appeal dismissed* 79 NY2d 978 [1992]; *Matter of Surface Line Operators Fraternal Org. v Tully*, 85 AD2d 858 [3d Dept 1981]). Furthermore, a presumption of correctness attaches to a notice issued by the Division, and the taxpayer must overcome this presumption (*see Matter of Suburban Carting Corp.*, Tax Appeals Tribunal, May 7, 1998, citing *Matter of Tavalacci v State Tax Commn.*, 77 AD2d 759 [3d Dept 1980]; *Matter of Leogrande*, Tax Appeals Tribunal, July 18, 1991, *confirmed* 187 AD2d 768 [3d Dept 1992], *lv denied* 81 NY2d 704 [1993]).

B. There is no dispute that the audit methodology utilized in this case was an indirect methodology and not based solely on the books and records of petitioner. In order for the Division to utilize an indirect methodology, it must show that it made an adequate request for books and records for the audit period (*see Matter of Christ Cella, Inc. v State Tax Commn.*, 102 AD2d 352 [3d Dept 1984]), and that it reviewed the records provided in order to determine that the records were inadequate for the purposed of conducting a complete audit (*see Matter of King Crab Rest. v Chu*, 134 AD2d 51 [3d Dept 1987]).

C. Both the July 16, 2012 and August 2, 2012 letters to petitioner constituted adequate requests for books and records and covered the entire audit period at issue. Pursuant to Tax Law

§ 1135 (a) (1), petitioner was required to keep records of every sale made and the tax payable on each sale. Additionally, petitioner admits that its records were inadequate.

D. While the Division may resort to an estimated or indirect audit method to calculate sales tax due where a taxpayer had failed to present books and records adequate for the Division to conduct a detailed audit (*see Matter of Urban Liqs. v State Tax Commn.*, 90 AD2d 576 [3d Dept 1982]), the method chosen by the Division must be reasonable (*see Matter of House of Audio of Lynbrook*, Tax Appeals Tribunal, January 2, 1992) and reasonably calculated to reflect the tax due (*see Matter of W.T. Grant Co. v Joseph*, 2 NY2d 196 [1957], *cert denied* 355 US 869 [1957]; *Matter of Ristorante Puglia v Chu*, 102 AD2d 348 [3d Dept 1984]). The method need not be exact (*Matter of Markowitz v State Tax Commn.*, 54 AD2d 1023 [3d Dept 1976], *affd* 44 NY2d 684 [1978]) and the auditor is given considerable latitude in devising an audit method (*Matter of Grecian Sq. v New York State Tax Commn.*, 119 AD2d 948 [3d Dept 1986]).

Petitioner did not submit any documents or present any witnesses to challenge the audit methodology used by the Division. Therefore, petitioner has failed to meet its burden of showing that the Division's audit method was not reasonably calculated to reflect taxes due or that the amount of tax assessed was erroneous.

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

F. The petition of Big Star Nunez Corporation is denied and the notice of determination, assessment number L-042694801, dated April 10, 2015, is sustained.

DATED: Albany, New York  
September 20, 2018

/s/ Donna M. Gardiner  
ADMINISTRATIVE LAW JUDGE