

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
ANIKA USA, INC. : DETERMINATION
 : DTA NO. 827903
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, 2013 through February 28, 2014. :

Petitioner, Anika USA, Inc., filed a petition for revision of a determination or for refund of sales and use taxes under articles 28 and 29 of the Tax Law for the period March 1, 2013 through February 28, 2014.

A hearing was held before Dennis M. Galliher, Administrative Law Judge, in New York, New York, on October 19, 2018, at 10:30 A.M., with all briefs to be submitted by January 28, 2019, which date began the six-month period for the issuance of this determination. Petitioner appeared by Arthur Morrison, Esq., and Irina Herman, CPA. The Division of Taxation appeared by Amanda Hiller, Esq. (Michael J. Hall, of counsel).

ISSUES

I. Whether the Division of Taxation clearly requested and received from the petitioner books and records that were sufficient for the conduct of an audit.

II. Whether, if sufficient books and records were not provided, petitioner has nonetheless established that its claimed nontaxable sales were indeed not subject to tax, such that the Division's imposition of tax thereon should be canceled.

III. Whether petitioner has established any bases justifying reduction or cancellation of the penalties assessed.

FINDINGS OF FACT

1. During the period at issue, petitioner, Anika USA, Inc., operated a watch and jewelry store located at 1177 B Broadway, New York, New York. Petitioner filed its sales and use tax returns on an annual basis. For the period at issue, spanning March 1, 2013 through February 28, 2014, petitioner reported gross sales of \$541,797.00, and taxable sales of \$27,211.00, leaving \$514,586.00 (or 94.9776%) of its sales claimed as nontaxable sales.

2. By a letter dated November 25, 2015, the Division of Taxation (Division) advised petitioner that a sales and use tax audit would be conducted for the audit period spanning March 1, 2012 through February 28, 2015. The Division's audit appointment letter explained that all books and records pertaining to petitioner's sales and use tax liability for the specified audit period must be made available, on or before December 7, 2015, for audit review.

3. The audit appointment letter was accompanied by an information document request (IDR # 1), listing the records required to be available for audit review. Among the records specifically requested were sales tax returns, worksheets and cancelled checks; federal income tax returns; New York State corporation tax returns; general ledger; general journal and closing entries; sales invoices; all exemption documents supporting nontaxable sales; chart of accounts; fixed asset purchase/sales invoices; expense purchase invoices; merchandise purchase invoices; bank statements, canceled checks and deposit slips for all accounts; cash receipts journal and sales journal; cash disbursements journal and purchase journal; the corporate book, including minutes, board of directors and articles of incorporation; depreciation schedules; and lease/rental agreements for the audit period.

4. By a letter dated November 30, 2015, petitioner's representative responded to the Division's appointment letter, seeking a postponement and additional time to gather the requested records. The Division's auditor granted this request by a letter dated December 4, 2015, and postponed the audit appointment to January 29, 2016, on which date petitioner's representative was to provide the requested records for review by the auditor.

5. Petitioner's representative cancelled the January 29, 2016 audit appointment. The Division's auditor made several more requests for records, both by telephone and in writing, but petitioner did not respond thereto. On February 3, 2016, petitioner's representative advised the auditor that she did not have any of the requested records, noted that petitioner's business had closed as of February 28, 2014, and therefore should not be subject to audit.¹

6. Following an additional unsuccessful attempt to contact petitioner's representative, the auditor prepared a statement of proposed audit change for sales and use tax (form AU-346). The auditor calculated additional sales tax due based on accepting petitioner's gross sales, as reported on its sales tax returns, but disallowing petitioner's claimed nontaxable sales for lack of any records in substantiation of such claimed nontaxability. On February 8, 2016, the auditor sent the form AU-346, with its proposed assessment, accompanied by another written request for records and a copy of IDR # 1, to petitioner, petitioner's representative, and to the two persons the auditor believed were under a duty, as petitioner's owners and/or officers, to provide records.

7. The auditor made several unsuccessful, additional attempts to contact petitioner's representative. On June 3, 2016, the auditor spoke with petitioner's representative by telephone, concerning the status of the audit, and again requested petitioner's records.

¹ The record indicates that at the start of the subject audit, a successor business, known as SK Global Trading, was being operated by petitioner's two owners at the same 1177 B Broadway premises where petitioner's business had operated (*see* finding of fact 18).

8. On July 15, 2016, the auditor's supervisor left a telephone voice mail message with petitioner's representative requesting a return call, but none was forthcoming. On the same date, the auditor's supervisor also spoke by telephone to one of petitioner's owners concerning the lack of any response by petitioner and its representative, including the failure to have provided any books or records as requested.

9. On July 15, 2016, the Division's auditor sent another written request, including another copy of IDR # 1, to petitioner, petitioner's representative, and to the two persons she believed were persons under a duty, as petitioner's owners and/or officers, to provide records for review. The auditor advised that if she received no response, and no records were provided, she would finalize her audit based upon available information.

10. The Division's auditor was never provided with any books or records during the audit, notwithstanding the foregoing described attempts to obtain the same.

11. Given the lack of records, the auditor calculated tax due as described above (*see* finding of fact 6). Specifically, the auditor accepted petitioner's gross sales of \$541,797.00, as reported on its sales and use tax return for the one-year period at issue herein, subtracted petitioner's taxable sales of \$27,211.00, as reported on such return for the same period, and thereby arrived at claimed nontaxable sales in the amount of \$514,586.00. The auditor deemed such claimed nontaxable sales to be taxable sales, for lack of any substantiation of nontaxability, utilized the applicable tax rate (8.875%), and determined additional tax due in the amount of \$45,669.52 on such claimed but unsubstantiated nontaxable sales for the period at issue.²

² The audit period spanned March 1, 2012 through February 28, 2015 (*see* finding of fact 2). The period at issue herein is a one-year portion of the audit period, spanning March 1, 2013 through February 28, 2014.

12. On August 5, 2016, the auditor mailed the form AU-346, together with her workpapers in support thereof, by certified mail, to petitioner, petitioner's representative, and to the persons believed to be under a duty to collect and pay over taxes on behalf of petitioner.

13. There was no response to the foregoing form AU-346 and, on September 29, 2016, the Division issued a notice of determination (Assessment No. L-045487236) to petitioner assessing additional sales tax due for the period March 1, 2013 through February 28, 2014 in the amount of \$45,669.52, plus penalty and interest.

14. Petitioner challenged the foregoing assessment, and at the hearing submitted:

a) a one-page workpaper from an earlier Division audit of petitioner showing additional sales tax due in the amount of \$179,568.70 for the period spanning June 1, 2009 through February 29, 2012.

b) a copy of a check in the amount of \$283,982.00," drawn on the "New York City Property Clerk Holding Account as Custodian," dated October 6, 2011, and made payable to "Shamin, Abdul Awal."³

c) a one-page spread sheet, listing 28 invoices by invoice number, dollar amount, vendor/customer name. All of the entries on the spread sheet list dates that fall in the months of June, July and August, 2010, i.e., prior to the period at issue herein. The spread sheet shows the "audit method" as "projected," and the "status" as "agreed."⁴

15. The purpose for submitting the foregoing items is not entirely clear. However, it seems such items were offered in support of the allegation that petitioner had provided complete and adequate records for an earlier audit. Petitioner maintains that the Division had such earlier-submitted records in its possession at the time the audit herein at issue was being conducted, and

³ Mr. Shamin is one of the two persons identified by the auditor as an owner and/or officer of petitioner. The other is Mohammed Uddin.

⁴ Three of the listed invoices appear to pertain to the same named vendor/customer, two include no vendor/customer name, and one lists simply "c" as the vendor/customer. No addresses were listed for any of the names appearing in the vendor/customer column. While the spreadsheet listed invoices, as described, no actual invoices were provided.

that notwithstanding petitioner's failure to have submitted records as requested for the period herein at issue, the Division was obliged to use and rely upon the records from the earlier audit, as well as the result of that audit, in the present matter.

16. The first of the above-described documents submitted by petitioner reveals the same to set forth a calculation of tax due for the period June 1, 2009 through February 29, 2012 (the earlier audit), based upon a review of claimed nontaxable sales for the three month test period spanning June, July and August, 2010, the calculation of an error rate based thereon, and a projection of additional tax due based on that error rate. More specifically:

- a) for the three month test period, petitioner reported nontaxable sales of \$588,711.00;
- b) per invoices provided to and reviewed by the auditor, substantiated nontaxable sales for the test period totaled \$350,221.60;
- c) the \$238,489.00 resulting difference between claimed versus substantiated non-taxable sales was treated as unsubstantiated claimed nontaxable sales;
- d) comparing unsubstantiated claimed nontaxable sales (\$238,489.40) to total reported nontaxable sales (\$588,711.00) yielded a 40.5104% error rate in reported taxable sales;
- e) applying the foregoing error rate (40.5104%) to total reported non-taxable sales for the period June 1, 2009 through February 29, 2012 ((\$4,994,543.00) resulted in additional taxable sales of \$2,023,309.35, with additional tax due thereon in the amount of \$179,568.70 (*see* finding of fact 14 [a]).

17. At hearing, petitioner also submitted 31 resale certificates (form ST-120), 28 of which are undated, and three of which bear a date that is before the period at issue. No additional evidence was provided with respect to any of these resale certificates.

18. Petitioner submitted a one-page attorney's letter, dated October 18, 2018, referencing a different corporation (SK Global Trading, Inc.), and involving a matter before the Division's Bureau of Conciliation and Mediation Services (BCMS). This letter was described as being submitted for purposes of "full disclosure." The record bears out that SK Global Trading, Inc., is

a successor entity, organized by petitioner's president, that operated at the same premises where petitioner operated its business. The purpose for this document is not further described, nor is there additional evidence to show any connection between the period herein at issue and the BCMS matter involving SK Global Trading, Inc.

19. Petitioner further provided documents to show that a search of petitioner's premises was conducted by the New York City Police Department, the Port Authority Police, and the New York County District Attorney, on August 18, 2010, pursuant to a search warrant (Warrant No. N 786-10), and that all of petitioner's books and records, including checkbooks, statements, records of bills and receipts, were seized as a result of that search. By a letter dated July 18, 2014, petitioner was advised to contact the Manhattan District Attorney's office to request return of the records. This letter indicated the records were seized on "indictment # 2580/11," and that the "criminal case was closed 10/25/11." In 2015, petitioner commenced an action to recover the seized items (Index No.; 151067/2015), but was advised by letter dated August 3, 2015, that the documents could not be located, and since the passage of the time within which to make a demand for return of the seized property had long passed, the same had likely been disposed of pursuant to law.⁵

20. Finally, petitioner submitted a copy of a Consent to Dissolution of a Corporation regarding Anika USA, Inc., dated as effective until April 27, 2015. Petitioner admitted that the dissolution was never filed with the New York Secretary of State, and that petitioner has not, in fact, been dissolved.

⁵ The record includes an inventory of the "items recovered placed on Property Clerk Invoice," dated December 9, 2010. This inventory does not describe the seized property in any manner other than by a sequential numerical listing labeled "R546065" through "R546490."

CONCLUSIONS OF LAW

A. The standard for reviewing a sales tax audit where an indirect audit methodology has been employed in arriving at an estimated determination of sales tax liability is well established, and was set forth in *Matter of AGDN, Inc.* (Tax Appeals Tribunal, February 6, 1997), as follows:

“a vendor . . . is required to maintain complete, adequate and accurate books and records regarding its sales tax liability and, upon request, to make the same available for audit by the Division (*see*, Tax Law §§ 1138[a]; 1135; 1142[5]; *see, e.g., Matter of Mera Delicatessen*, Tax Appeals Tribunal, November 2, 1989). Specifically, such records required to be maintained ‘shall include a true copy of each sales slip, invoice, receipt, statement or memorandum’ (Tax Law § 1135). It is equally well established that where insufficient records are kept and it is not possible to conduct a complete audit, ‘the amount of tax due shall be determined by the commissioner of taxation and finance from such information as may be available. If necessary, the tax may be estimated on the basis of external indices . . . ’ (Tax Law § 1138[a]; *see, Matter of Chartair, Inc. v. State Tax Commn.*, 65 AD2d 44, 411 NYS2d 41, 43).

When estimating sales tax due, the Division need only adopt an audit method reasonably calculated to determine the amount of tax due (*Matter of Grant Co. v. Joseph*, 2 NY2d 196, 159 NYS2d 150, *cert denied* 355 US 869); exactness is not required (*Matter of Meyer v. State Tax Commn.*, 61 AD2d 223, 402 NYS2d 74, *lv denied* 44 NY2d 645, 406 NYS2d 1025; *Matter of Markowitz v. State Tax Commn.*, 54 AD2d 1023, 388 NYS2d 176, *affd* 44 NY2d 684, 405 NYS2d 454). The burden is then on the taxpayer to demonstrate, by clear and convincing evidence, that the audit method employed or the tax assessed was unreasonable (*Matter of Meskouris Bros. v. Chu*, 139 AD2d 813, 526 NYS2d 679; *Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451).”

B. When a sales tax return is not filed, or is incorrect or insufficient, the amount of tax due can be determined, as above, from the information available, and may be estimated (*see* Tax Law §1138 [a] [1]). The well-established standard for reviewing sales tax audits where the Division resorts to indirect auditing methods, including the use of estimates, 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 Ligs. 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).”

C. In this case, the record establishes that the Division made numerous clear and unequivocal written and oral requests for petitioner’s books and records, including records in substantiation and verification of petitioner’s claimed nontaxable sales. In response, petitioner failed to provide any records pertaining to the period at issue. Instead, petitioner claimed that its business had ceased operations by the time the audit commenced and, consequently, that it should not be subjected to an audit. Petitioner also alleged that complete, exact, and precise records were supplied to the Division during a prior audit, that the Division had the same in its possession at the time of the audit at issue herein, and that the auditor should have used these records, or the result derived therefrom during the prior audit, for purposes of the audit at issue herein.

D. Given that petitioner provided no records at all for purposes of the subject audit, the Division was unable to confirm that petitioner’s claimed nontaxable sales for such period were, in fact, not subject to tax. Under these circumstances, the Division accepted petitioner’s gross

sales and taxable sales, as reported, but disallowed the claim that the balance of its sales were nontaxable sales, for lack of substantiation thereof. Accordingly, the Division issued the notice of determination numbered L-045487236, based on petitioner's failure to have provided any records or other basis upon which to verify the claim, per petitioner's sales and use tax return as filed for the period at issue, that \$514,586.00 (94.9776%), or any other amount of its sales, were not, in fact, taxable sales.

E. Pursuant to Tax Law § 1132 (c) (1), petitioner bears the burden of proving that the tax assessed was erroneous (*Matter of Rizzo v Tax Appeals Trib. of State of N.Y.*, 210 AD2d 748 [3d Dep +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 Tavolacci 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]). In response to the Division's assessment of additional tax, petitioner has continued to maintain the positions that it was not properly subject to audit because it had ceased operations as of the start of the audit, and that the Division should have utilized assertedly complete, exact and precise records allegedly already in its possession from a prior audit, in order to determine whether petitioner's return for the subsequent period at issue herein correctly reported petitioner's taxable sales and its tax liability for such subsequent period.

F. Petitioner's arguments are rejected. First, petitioner simply did not provide any documents for the period at issue, or present any witnesses at hearing, to support or to verify that

any portion of its claimed nontaxable sales were, in fact, not subject to tax. In the absence of any such evidence in support of claimed nontaxable sales, the Division is under no obligation to guess at the portion of a vendor's sales, if any, that are, or might possibly be, nontaxable (*see* Tax Law § 1132 [c] [1]). Further, petitioner's assertion that complete records for the prior audit were in the Division's possession, and should have been used for this audit, is rejected. Initially, there is no proof to support the allegation that the Division remained in possession of any of petitioner's substantiating records that may have been submitted in connection with a prior audit. In fact, testimony at hearing supports a contrary conclusion. Moreover, review of the evidence in the record concerning that earlier audit belies any claim that complete, exact and precise records in substantiation of claimed nontaxable sales for such earlier period were in fact provided by petitioner. To the contrary, that earlier audit itself utilized a test period wherein petitioner was unable to provide substantiation with regard to the nontaxable status of over forty percent of its claimed nontaxable sales (*see* finding of fact 16). Essentially, petitioner seems to claim that, notwithstanding the absence of any records for the period currently under audit, the Division is somehow required to rely upon and apply the results of a prior audit for purposes of estimating the amount of tax that is due for a later audit period. Such an argument is, at best, akin to imposing a requirement upon the Division that it must accept and apply a previous estimated audit methodology and result, so as to reduce or eliminate an assessment of tax otherwise determined for a later period. The Division is simply under no such obligation, and this argument is rejected both as a general proposition (*see Matter of Markowitz v State Tax Comm'n; Matter of S.H.B. Super Markets, Inc v Chu*, 135 AD2d 1048 [3d Dept 1987]), and absolutely in a case such as this where the taxpayer fails to provide any books and records on audit (*see Matter of AGDN, Inc.*).

G. Petitioner's argument that its records were seized pursuant to a search warrant, were in the custody of law enforcement authorities or had been subsequently disposed of by such authorities, and thus were not available to be provided at the time of the subject audit or thereafter at hearing, is of no assistance here (*see* finding of fact 19). In fact, the August 18, 2010 date of the search and seizure falls well before the period at issue. Hence, the records seized would pertain to periods prior to the audit period at issue herein. There is no explanation offered, nor is it in any manner apparent, how records for a prior period would be applicable or relevant to petitioner's claimed nontaxable sales allegedly made during a period subsequent to the search and seizure. There is no indication that petitioner made any efforts to go back to its customers for documents concerning previously made sales, notwithstanding the argument that many of petitioner's customers made purchases during both the prior and the current audit periods. In this regard, there is no claim or evidence that petitioner had or maintained any blanket exemption certificates for any of its alleged repeat customers.⁶ The overriding question is why there were no records in substantiation of claimed nontaxable sales available or provided for the period here at issue. The search and seizure of records pertaining to a prior period provides no answer to this question, nor does it indicate that records for the current period were unavailable for presentation upon audit due to circumstances beyond petitioner's control. Under all of the circumstances presented herein, the Division's audit method and result must be upheld.

H. Finally, the Division's imposition of penalty in this matter is sustained. Petitioner has advanced no basis in explanation of its failure to have maintained or made available records for

⁶ Petitioner's statement that the "customers were all the same," without any evidence to support that petitioner made recurring sales to repeat purchasers under some form of blanket exemption, leaves this claim entirely unavailing. Indeed, having had its records seized should, if anything, have heightened an awareness of the need for petitioner to have obtained and maintained substantiation in support of the exempt status of its purchasers and their purchases going forward.

the period at issue, or in support of its claimed but unsubstantiated nontaxable sales, nor has petitioner advanced any explanation or support for a conclusion that the underpayment of tax herein was beyond the control of the petitioner and not due to any fault on its part (*see Matter of F & W Oldsmobile, Inc. v New York State Tax Commission*, 106 AD2d 792 [3d Dept 1984]). Accordingly, petitioner has not met its burden to show that there was reasonable cause for its failures such that penalty is not appropriate and should be abated (*see Matter of A & V Crown, Inc.*, Tax Appeals Tribunal, May 24, 1990).

I. The petition of Anika USA, Inc., is hereby denied and the notice of determination dated September 26, 2016 is sustained.

DATED: Albany, New York
July 25, 2019

/s/ Dennis M. Galliher
ADMINISTRATIVE LAW JUDGE