STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition of **SHAWN MCKEE ENTERPRISES, INC.** 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, 2010 through February 29, 2016.	:	DETERMINATION DTA NO. 828734

Petitioner, Shawn McKee Enterprises, 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, 2010 through February 29, 2016.

A hearing was held before Donna M. Gardiner, Administrative Law Judge, in New York, New York, on March 11, 2020 at 10:30 a.m., with all briefs to be submitted by August 21, 2020, which date began the six-month period for issuance of this determination. Petitioner appeared by Sales Tax Defense LLC (Jennifer Koo, Esq., of counsel).[1] The Division of Taxation appeared by Amanda Hiller, Esq. (Adam L. Roberts, Esq., of counsel).

ISSUES

I. Whether petitioner's sales of sulfuric acid qualify as sales for resale.

II. If not, whether petitioner, in good faith, timely accepted properly completed resale certificates from its customers.

[1] By letter filed on December 2, 2020, the Division of Tax Appeals was informed that the representative has withdrawn all representation of petitioner in this matter moving forward.

III. Whether petitioner has demonstrated reasonable cause such that penalties should be abated.

FINDINGS OF FACT

1. Petitioner, Shawn McKee Enterprises, Inc., is located at 3698B Horseblock Road in Medford, New York. It is in the business of selling sulfuric acid to contractors who perform cesspool cleaning for their customers. Petitioner was not registered to collect sales tax in New York State. Petitioner's position is that it is engaged in sales for resale of the sulfuric acid and, as such, its sales are nontaxable.

2. The Division of Taxation (Division) began an audit of petitioner in March of 2016. The audit period was March 1, 2010 through February 29, 2016. On March 21, 2016, the Division made a request for books and records to petitioner through an information document request. This request explained that certain documents were required to be provided to the Division which included all exemption documents supporting petitioner's claimed non-taxable sales such as resale certificates and capital improvement certificates.

3. There were 38 resale certificates presented on audit. One certificate was dated within the audit period. The remaining certificates were either undated or dated after the information document request was made by the Division. The resale certificates that had a description of service listed on the form states either maintenance/cleaning/cesspool services or liquid waste services.

4. The Division concluded that petitioner was an unregistered vendor in New York State engaged in the sale of taxable tangible personal property. As such, it issued a notice of determination, assessment number L-045870653, dated December 28, 2016, to petitioner for

additional sales and use taxes due for the audit period in the amount of $479,539.35 plus interest and applicable penalties, including a penalty for operating without a certificate of authority.

5. Petitioner filed a request for a conciliation conference at the Bureau of Conciliation and Mediation Services in protest of the notice. By conciliation order, CMS #273947, dated March 16, 2018, the notice was sustained in full.

6. On May 25, 2018, petitioner timely filed its petition with the Division of Tax Appeals in protest of the conciliation order.

7. At the hearing, the auditor testified to the work performed during his audit and explained the basis for his conclusion that petitioner was liable for sales tax on sales of tangible personal property, i.e., sulfuric acid, to cesspool companies in their performance of cleaning or maintenance services.

8. The auditor stated that he was told petitioner sold acid, yet in his review of the resale certificates presented to him, he found the acid was purchased by contractors for use in cleaning services. Additionally, the auditor noted that most of the resale certificates were dated after the audit period. The auditor indicated in his report that, in a situation where tangible personal property is sold for resale, he would expect petitioner's customers to be retail stores that would resell the sulfuric acid as is. The auditor did not find any evidence of sales to retail stores.

9. Moreover, the auditor testified that all the resale certificates accepted by petitioner were forms ST-120s. The auditor stated that the instructions on this form explicitly limit the use of the form and that contractors cannot use forms ST-120. The instructions state that a contactor must use either form ST-120.1, Contractor Exempt Purchase Certificate or form AU-297, Direct Payment Permit or pay the sales tax (***see*** exhibit F).

10. The auditor stated that in discussions he had with petitioner's initial representative, the representative conceded that petitioner was required to register as a vendor with New York State, to file for a certificate of authority and to start charging sales tax. Thereafter, petitioner registered with the State. However, there remained a disagreement over the amount of sales tax owed for the audit period.

11. The auditor was questioned on cross-examination regarding the existence of two separate statements of proposed audit changes (form AU-346) that were issued to petitioner during the audit that asserted much different amounts of additional sales tax. The auditor noted that petitioner's representative had changed during the audit. The auditor's notes indicated that during initial discussions, a form AU-346, dated July 28, 2016, had been issued and then subsequently rescinded. Petitioner's representative questioned him about this form AU-346.[2] Specifically, she asked the auditor to explain why the subsequent form AU-346 asserted tax on all of petitioner's sales of sulfuric acid rather than the original form AU-346 which assessed tax on only half the total sales made by petitioner. The auditor explained that the original form AU-346 was prepared for settlement purposes only. It is noted that on page 35 of exhibit E, there is correspondence, dated August 22, 2016, from the auditor to petitioner's second representative explaining that the initial form AU-346 was rescinded.

12. Petitioner presented the testimony of Eric McKee, president of petitioner. Mr. McKee explained the cesspool cleaning industry. Specifically, he testified about the use of sulfuric acid in cleaning cesspools. He stated that petitioner's customers use the sulfuric acid, not directly in the septic tanks, but in the overflow cesspool. He testified that the sulfuric acid is twice as heavy as water and the chemicals will descend to the bottom of the cesspool where they

[2] It is noted that petitioner's representative at hearing did not represent it during any part of the audit.

target a clog. The sulfuric acid heats up and causes a chemical reaction that breaks up the clog which eventually leaches through the sand and turns it into clean water again. Mr. McKee testified that the sulfuric acid takes approximately 72 hours to work once placed into the cesspool.

13. Mr. McKee acknowledged that petitioner did not operate with a certificate of authority from New York State during the audit period.

14. Mr. McKee testified regarding his acceptance of resale certificates from his customers. He explained that he always received timely resale certificates, forms ST-120, for sales of sulfuric acid. Specifically, he stated that "[w]hen a company comes into my business and asks me to sell them sulfuric acid, I ask them for a resale certificates [sic], and when I receive their resale certificates, I sell them sulfuric acid." When asked to explain the absence of resale certificates on audit, he testified that his office was robbed on May 15, 2014, and the resale certificates were among the many items stolen. However, Mr. McKee failed to explain the absence of timely accepted resale certificates for the period after the robbery, i.e., May 15, 2014 through February 29, 2016. Mr. McKee stated that when this audit began, his initial representative explained that Mr. McKee should recreate the stolen resale certificates and to ensure that these replacements were made available to the auditor. Mr. McKee identified 29 resale certificates as the replacement resale certificates that he created for the purposes of the audit. These are all in evidence as exhibit 4.

15. The record contains resale certificates in three separate exhibits. Exhibit E, the auditor's workpapers at pages 170-207, contains 38 forms ST-120 and exhibit 2 contains the exact same forms ST-120. In contrast, exhibit 4 contains 29 forms ST-120 that Mr. McKee testified were replacements for those stolen during the robbery. This characterization is, at best,

inaccurate. In a review of exhibit 4, there are 24 resale certificates that were recreated from the existing forms ST-120 presented to the auditor, all dated after the audit period, and contained in exhibits E and 2. However, it is interesting to note that Part 1 of the form is not completed consistently. Form ST-120 requires the purchaser to indicate what is being purchased. There are two options: option A is the purchase of tangible personal property for resale or option B indicates that the purchaser is selling a service. In exhibits E and 2, 36 of the forms ST-120 indicate that the purchasers chose option B, demonstrating the sale of a service. In exhibit 4, all 29 forms ST-120 indicate the purchaser chose option A, a purchase of tangible personal property for resale, in direct contradiction of exhibits E and 2. Clearly, exhibit 4 was not an attempt to merely recreate the stolen resale certificates, but rather, a deliberate act to alter the forms ST-120 presented during the audit to bolster petitioner's argument that its sales of the sulfuric acid were sales for resale.

16. Mr. McKee also testified that he knew that some of the cesspool companies were selling sulfuric acid directly to homeowners. Petitioner submitted 14 invoices that are dated within the audit period to support his understanding that his purchasers were selling sulfuric acid directly to homeowners. However, a review of the invoices show that each sale consisted of a service of pumping a cesspool. Additionally, it was never explained how petitioner obtained these invoices dated during the audit period.

17. Petitioner also presented the testimony of Mark Stone, CPA. He was questioned regarding his perception of the vendor protection rights afforded to vendors who accept a resale certificate in good faith. Mr. Stone was not involved in the audit of petitioner. His testimony was general in nature and he testified that much of his knowledge about the case was based on discussions that he had with petitioner's second representative who was involved with the audit.

At no point did Mr. Stone speak with Mr. McKee concerning the decisions made by petitioner to not register as a vendor or to accept the incorrect resale certificates by its purchasers who were all contractors.

CONCLUSIONS OF LAW

A. Tax Law § 1105 (a) imposes a sales tax on the receipts from "every retail sale" of tangible personal property. Tax Law § 1101 (b) (4) (i) defines retail sale as:

> "[a] sale of tangible personal property to any person for any purpose, other than (A) for resale as such or as a physical component part of tangible personal property, or (B) for use by that person in performing the services subject to tax under paragraphs (1), (2), (3), (5), (7) and (8) of subdivision (c) of section eleven hundred five where the property so sold becomes a physical component part of the property upon which the services are performed or where the property so sold is later actually transferred to the purchaser of the service in conjunction with the performance of the service subject to tax. *Notwithstanding the preceding provisions of this subparagraph, a sale of any tangible personal property to a contractor, subcontractor or repairman for use or consumption in erecting structures or buildings, or building on, or otherwise adding to altering, improving, maintaining, servicing or repairing real property, property or land, as the terms real property, property or land are defined in the real property tax law, is deemed to be a retail sale regardless of whether the tangible personal property is to be resold as such before it is so used or consumed . . .*" (emphasis added).

It is presumed that all receipts for sales of tangible personal property are subject to tax until the contrary is established, and the burden of proving that any receipt is not taxable will be upon the person required to collect the tax or the customer (Tax Law § 1132 [c]; ***Matter of Rizzo v Tax Appeals Trib. of State of N.Y.***, 210 AD2d 748 [3d Dept 1994]).

B. The presumption of taxability created by Tax Law § 1132 (c) is rebuttable (see ***Matter of RAC Corp. v. Gallman***, 39 AD2d 57 [Dept. 1972]). The regulations of the Commissioner provide that the failure to receive a timely exemption certificate does not alter the tax status of the transaction (20 NYCRR 532.4 [6]). Rather, when there has been a timely protest of a notice of determination, the vendor retains the right to establish that the transaction is nontaxable (20

NYCRR 532.4 [6]). However, the vendor will be unable to rely solely upon the exemption certificate to establish that it was unnecessary to collect tax (***id.***). Thus, the specific question is whether petitioner has provided sufficient evidence that the sales of sulfuric acid to cesspool cleaning companies were sales for resale and not subject to tax.

C. Petitioner does not dispute that all its sales are to contractors that provide cesspool cleaning services. Tax Law § 1105 (c) (5) imposes a sales tax on the receipt of every sale of a service for maintaining, servicing or repairing real property.

D. Petitioner argues that its sales of sulfuric acid qualify as sales of tangible personal property for resale. This argument is without merit. Primarily, petitioner only sold sulfuric acid to cesspool cleaning companies. The service provided by its customers is taxed pursuant to Tax Law § 1105 (c) (5). Additionally, in the definition of retail sale, as set forth in Tax Law § 1101 (b) (4) (i), the statute explicitly states that a sale of any tangible personal property to a contractor for "maintaining, servicing or repairing real property, property or land . . . is deemed to be a retail sale regardless of whether the tangible personal property is to be resold as such before it is so used or consumed . . . ." Therefore, since petitioner's customers were all contractors, the statute clearly states that any tangible personal property sold to its customers are subject to sales tax. It is also noted that 36 purchasers who bought sulfuric acid from petitioner indicated on the resale certificates that they were providing a service.

E. Petitioner relies on ***Matter of Finch, Pruyn v Tully*** (69 AD2d 193 [3d Dept 1979]) in support of its argument. In ***Finch, Pruyn***, it was determined that chemicals used in the production of paper were sales for resale, where the chemicals were actually transferred to the purchaser. In this case, the sulfuric acid sold by petitioner was used in maintaining or servicing real property which is an explicit retail sale subject to tax regardless of how the sulfuric acid is

used or consumed (***see*** Tax Law § 1101 [b] [4] [i]). Therefore, ***Finch, Pryun*** is inapplicable to the facts of this case.

F. As it has been determined that the sales in question were not sales for resale, the next issue to address is whether petitioner has demonstrated that it accepted resale certificates from its customers in good faith. The regulation at 20 NYCRR 532.4 (b) provides, in pertinent part, that:

> "(2) A vendor who in good faith accepts from a purchaser a properly completed exemption certificate or, as authorized by the Department, other documentation evidencing exemption from tax not later than 90 days after delivery of the property or the rendition of the service is relieved of liability for failure to collect the sales tax with respect to that transaction. The timely receipt of the certificate or documentation itself will satisfy the vendor's burden of proving the nontaxability of the transaction and relieve the vendor of responsibility for collecting tax from the customer.
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> (i) a certificate or other document is 'accepted in good faith' when a vendor has no knowledge that the exemption certificate or other document issued by the purchaser is false or is fraudulently presented. If reasonable ordinary due care is exercised, knowledge will not be imputed to the seller required to collect the tax.
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> * * *
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> (3) When a vendor has met the criteria in paragraph (2) of this subdivision, it is protected from liability for failure to have collected tax from the purchaser and the burden of proving the nontaxability of such transaction rests solely on the purchaser.
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> * * *
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> (5) A vendor is not relieved of the burden of proof when it failed to obtain an exemption certificate or accepted an improper certificate, or had knowledge that the exemption certificate issued by the purchaser was false or fraudulently presented."

Petitioner argues that the resale certificates were timely received, properly completed and accepted in good faith. Therefore, petitioner asserts that it should be absolved of any liability for the collection of the sales tax due in this case.

G. Primarily, petitioner failed to prove that the ST-120s were timely received. As set forth in finding of fact 3, only one of the resale certificates was for a transaction that occurred during the audit period. Mr. McKee alleged that he always accepted resale certificates at the time of the sale. He explained that all his resale certificates were included in items stolen from the business during a robbery in May of 2014. However, the robbery fails to shed light on the lack of resale certificates for the period following the robbery up through the conclusion of the audit period.

Mr. McKee testified that his initial representative explained that he should recreate any of the resale certificates that were allegedly stolen during the audit period. However, as discussed above in finding of fact 15, the purported recreated certificates were all just reproduced, altered copies of the certificates provided on audit. There was only one certificate from the audit period. Clearly, petitioner failed in its burden to establish the timely acceptance of resale certificates.

H. Assuming that petitioner was determined to have timely accepted the resale certificates, petitioner failed to show that the forms were properly completed. Forms ST-120 cannot be used by contractors. As set forth in finding of fact 9 and exhibit F, use of the form ST-120 states limitations for contractors. The auditor testified that the instructions clearly state that contractors cannot use form ST-120. The instructions provide three options for contractors; directing them to use form ST-120.1, Contractor Exempt Purchase Certificate, form AU-297, Direct Payment Permit or pay the sales tax at the time of purchase. Therefore, it is concluded that petitioner failed to demonstrate that the resale certificates were properly completed.

I. Petitioner argues that the resale certificates were accepted in good faith. The regulation provides, in pertinent part, that a certificate is accepted in good faith "when a vendor has no knowledge that the exemption certificate . . . issued by the purchaser is false or fraudulently presented. If reasonable ordinary due care is exercised, knowledge will not be

imputed to the seller required to collect the tax" (20 NYCRR 532.4 [b] [2] [i]). In light of the fact that petitioner did not timely accept the resale certificates and that it accepted the wrong forms from its customers, such factors militate against a finding that petitioner accepted the forms ST-120 in good faith. Additionally, petitioner did not provide any testimony that it exercised ordinary due care or took any steps, as the vendor, to ascertain the appropriate resale certificate that was required for sales of sulfuric acid to customers. Accordingly, petitioner has failed to establish that it can be relieved of its responsibility for collecting the sales tax from its customers.

J. Tax Law § 1145 (a) (1) imposes penalties on taxpayers who fail to pay sales tax when due. However, if such failure to pay sales tax was a result of reasonable cause and not due to willful neglect, such penalties may be abated (***see*** Tax Law § 1145 [a] [1] [iii]). In establishing reasonable cause for penalty abatement, the taxpayer faces an onerous task (***see Matter of Philip Morris, Inc.***, Tax Appeals Tribunal, April 29, 1993). Petitioner argues that it was justified in its position that its sales of sulfuric acid were sales for resale. However, petitioner did not explain its failure to register as a vendor in New York State nor what resources were relied upon in determining that it could accept resale certificates from contractors on sales of sulfuric acid. As explained by the auditor during his testimony, and the notes included in the audit report, it was clear from petitioner's initial representative that not only should petitioner have registered as a vendor for sales tax, but the sales of sulfuric acid to contractors were taxable to the contractors for use in providing the service of cleaning cesspools. Petitioner is unable to point to anything that it relied upon in making its determination to accept forms ST-120 from its customers. Accordingly, the penalties are sustained.

K. The petition of Shawn McKee Enterprises, Inc., is denied and the notice of determination #L-045870653 dated December 28, 2016, is sustained in full.

DATED: Albany, New York

February 18, 2021

/s/ Donna M. Gardiner
ADMINISTRATIVE LAW JUDGE