ALABAMA TAX TRIBUNAL

HODA MARKET, LLC,	§	
Taxpayer,	§	DOCKET NOS COUNTY 18-104-JP
v.	§	S. 18-719-JP
TUSCALOOSA COUNTY SPECIAL TAX BOARD	§	
	§	
and	§	
HODA MARKET, LLC, AND ITS SOLE MEMBER, AHMED ALATASSI,	§	
Taxpayer,	§	
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	
	§	

OPINION AND FINAL ORDER

The Alabama Department of Revenue performed a sales-tax audit of Hoda Market, LLC (Taxpayer), which is a convenience store and gas station located in Tuscaloosa County, Alabama. After the audit, the Revenue Department entered a final assessment of state sales tax against the Taxpayer and its sole member, Ahmed Alatassi, for the periods of February 2014 through March 2017. The assessment totaled $187,657.92, which included tax, interest, a late-payment penalty, and the fraud penalty. The Revenue Department shared its audit findings with the Tuscaloosa County Special Tax Board which, on behalf of Tuscaloosa County, entered a final assessment of local sales tax against the Taxpayer. The county assessment totaled $125,090.50 and included tax, interest, and a late-payment penalty.

The Taxpayer separately appealed each final assessment to the Alabama Tax Tribunal. The appeals were consolidated, and a hearing was conducted in 2019 involving all parties. Post-hearing briefs were filed by the Taxpayer, and a joint brief was filed by the tax agencies.

Questions Presented

1) Whether the Taxpayer proved that the Revenue Department erred in estimating the Taxpayer's taxable sales?

2) Whether the Revenue Department proved that the Taxpayer's underpayment of tax was fraudulent?

Law

Alabama law imposes a privilege or license tax – known as the sales tax – on those who are "engaged . . . in the business of selling at retail any tangible personal property whatsoever. . ." *See* Ala. Code § 40-23-2(1). The seller is required to add the tax to the sales price of the item and collect the tax from the purchaser, pursuant to Ala. Code § 40-23-26(a). Then, the seller is required to report and remit the tax, usually monthly. Ala. Code § 40-23-7(a).

The pertinent statutes regarding the Revenue Department's audit and assessment functions read as follows:

> (1) In addition to all other recordkeeping requirements otherwise set out in this title, taxpayers shall keep and maintain an accurate and complete set of records, books, and other information sufficient to allow the department to determine the correct amount of value or correct amount of any tax, license, permit, or fee administered by the department. . .
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> (2) The department may examine and audit the records, books, or other relevant information maintained by any taxpayer or other person for the purpose of computing and determining the correct amount of value or correct amount of any tax, license, or fee administered by the department. . .

Ala. Code § 40-2A-7(a)(1) – (2).

> (b) *Procedures governing entry of preliminary and final assessments; appeals therefrom.*
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> (1) ENTRY OF PRELIMINARY ASSESSMENT; FINAL ASSESSMENT OF UNCONTESTED TAX; EXECUTION OF PRELIMINARY AND FINAL ASSESSMENTS.
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> a. If the department determines that the amount of any tax as reported on a return is incorrect, or if no return is filed, or if the department is required to determine value, the department may calculate the correct tax or value based on the most accurate and complete information reasonably obtainable by the department. The department may thereafter enter a preliminary assessment for the correct tax or value, including any applicable penalty and interest.
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> (2) TIME LIMITATION FOR ENTERING PRELIMINARY ASSESSMENT.
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> Any preliminary assessment shall be entered within three years from the due date of the return, or three years from the date the return is filed with the department, whichever is later, or if no return is required to be filed, within three years of the due date of the tax, except as follows:
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> a. A preliminary assessment may be entered at any time if no return is filed as required, or if a false or fraudulent return is filed with the intent to evade tax.
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> b. A preliminary assessment may be entered within six years from the due date of the return or six years from the date the return is filed with the department, whichever is later, if the taxpayer omits from the taxable base an amount properly includable therein which is in excess of 25 percent of the amount of the taxable base stated in the return.
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> . . .

Ala. Code § 40-2A-7(b)(1) – (2).

> (d) *Underpayment due to fraud.* If any part of any underpayment of tax required to be shown on a return is due to fraud, there shall be added to the tax an amount equal to 50 percent of that portion of the underpayment which is attributable to fraud.

> For purposes of this section, the term "fraud" shall have the same meaning as ascribed to the term under 26 U.S.C. Section 6663, as in effect from time to time.

Ala. Code § 40-2A-11(d).

Facts

The Taxpayer's sole member, Mr. Ahmed Alatassi, testified that he moved to the United States (to the City of Tuscaloosa, Alabama) in 2001 at age 18 or 19. For the next 13 years, he worked in convenience stores and he opened a restaurant and a car business. For the first two or three years in those businesses, his roles included sales-tax responsibilities. Then, he opened the Taxpayer in 2014.

Mr. Alatassi stated that, during the audit period, the Taxpayer charged its customers 9% sales tax when they made purchases and that the tax was added to its customers' total sales amounts. The Taxpayer's cash register was equipped with "z-tapes" to record sales and every sale would have been run through the register and recorded on the z-tapes. In fact, Mr. Alatassi testified that no sales were made that were not recorded by the cash register. Before sale-tax returns were due for each month, the Taxpayer determined an amount to report as the taxable measure and then provided that number to his accountant who prepared returns based solely on what the Taxpayer reported to her. However, the Taxpayer did not report its gross receipts or gross sales amounts – the amounts on which it had charged sales tax to its customers – as the taxable measure on its returns. Instead, the Taxpayer reported the net amount of cash remaining in its bank account after paying bills.

Mr. Alatassi testified that he used the money from customers' debit and credit card purchases to pay his gasoline suppliers. "I never took the credit or debit to my pocket. It

goes to the gas supplier because we get ten days' credit." With some of the cash received from customers, the Taxpayer paid its employees and paid a few vendors who would accept cash payments. The remaining cash was deposited into the Taxpayer's bank account and the Taxpayer wrote checks to pay the remaining vendors, plus overhead expenses such as rent and utilities. After all expenses of the business were paid each month, the Taxpayer reported its taxable sales as the net amount remaining in its bank account. The amounts reported on the sales-tax returns never were based on the total sales that were processed through the cash register.

Mr. Alatassi testified that he had no policy of maintaining business records during the audit period and that he disposed of records sometimes daily. Obviously, he did not refer to sales records when determining the amounts to report as taxable sales on the returns. "I normally thought when you put the money in the bank, usually have a better record than everything else." At the hearing, though, the Taxpayer introduced z-tapes for the month of November 2015 and a summary of October and November 2015 sales (Taxpayer's Exhibits 1 and 2). Also, Mr. Alatassi stated that he did not intentionally hide the Taxpayer's sales numbers.

Ms. Dorothy Poe performed the audit for the Revenue Department. She testified that she requested all records from the Taxpayer that related to filing the Taxpayer's sales-tax returns, such as bank statements with cancelled checks, income tax returns, monthly worksheets, and cash register z-tapes. However, the Taxpayer provided only some bank statements (with no cancelled checks), a few purchase invoices, a few worksheets that contained merely the amounts reported on the returns, actual z-tapes for January,

February, and March 2017, and a 2014 federal income tax return. Ms. Poe then subpoenaed the Taxpayer's bank statements and cancelled checks. She also obtained invoices from the Taxpayer's vendors that showed the items and amounts purchased by the Taxpayer for resale.

Ms. Poe compared the monthly amounts spent by the Taxpayer on items for resale during the audit period with the amounts reported on the sales-tax returns and noticed that the purchases exceeded reported sales by more than $2.2 million. Specifically, the Taxpayer purchased for resale $2,774,286.25 worth of supplies from vendors, but reported total sales during that same period of only $553,266. (The auditor estimated purchases for two vendors, because she did not have purchase invoices from those two.)

Once the auditor determined that the Taxpayer's records were inadequate, she performed a classified purchase mark-up audit. Based on each vendor's most recent records, she listed each item purchased by the Taxpayer for resale and the wholesale price paid by the Taxpayer for that item. She then checked the Taxpayer's retail-sales price for each of those items by visiting the store. She calculated the mark-up percentage for each item by subtracting the Taxpayer's cost from the Taxpayer's retail-sales price (which represents profit) and then dividing the Taxpayer's profit by the cost of the item. To determine the average mark-up percentage by vendor, she applied that same two-step process to the total costs per the vendor's invoice and the total retail-sales prices of the corresponding items. Ms. Poe then applied that average mark-up percentage to the amount of the Taxpayer's purchases from each vendor during the audit period as shown on the invoices. The average mark-up percentage for all vendors was 24.5%. (The standard

IRS markup for this type of business is 35%.)

Applying the mark-up percentages to the Taxpayer's wholesale purchases, the auditor estimated the Taxpayer's total taxable measure during the audit period to be $3,453,846.13, which showed an underreporting by the Taxpayer of approximately $2.9 million. In other words, according to the Revenue Department's estimation, the Taxpayer underreported its taxable sales by about 84%.

Ms. Poe acknowledged that the Taxpayer provided some z-tapes during the audit for the months of January, February, and March 2017. However, when asked by the Tax Tribunal why the z-tape numbers would not be better to use than her estimates, she testified that the Taxpayer's wholesale purchases for those three months exceeded the amounts of sales shown on the z-tapes for those same months. She also noted that, for the four months immediately following the audit period, the Taxpayer's reported taxable sales increased dramatically. During the audit period, the Taxpayer reported an average of approximately $14,500 per month in taxable sales. After the audit period, however, that number increased to an average of approximately $50,400 per month. Mr. Alatassi attributed that increase to a change in accountants and to his reliance on z-tapes.

Analysis

Estimating Taxable Sales

The Taxpayer was required by law to maintain a complete set of records from which the correct amount of its sales-tax liability could be determined. Ala. Code § 40-2A-7(a)(1). Here, though, the Taxpayer admittedly maintained almost no records. Consequently, the Revenue Department was authorized to determine the correct amount of tax that should

have been reported "based on the most accurate and complete information reasonably obtainable..." Ala. Code § 40-2A-7(b)(1)a.

The Taxpayer argues in its brief that the final assessment should be adjusted by using actual sales numbers from the October and November 2015 z-tapes that it introduced at the hearing. More specifically, the Taxpayer disagrees with the auditor's mark-up method because it does not take into account inflation; *i.e.,* it was based on retail prices from May of 2017 to mark up sales for years 2014, 2015, and 2016. Instead, the Taxpayer argues that inflation rates from the Consumer Price Index should be factored in, which would result in lower mark-up percentages for the audit years. "This means the net retail price created by the auditor in 2017 *could* be 5.1% higher than the actual net retail amount used by the taxpayer during 2014. As a result, the 2014 audit mark ups should be decreased by 5.1%, the 2015 mark up should be decreased by 3.5%, and the 2016 mark up should be decreased by 3.4%." Taxpayer's Post Hearing Brief, 4 (emphasis added).

Concerning the z-tape numbers for October and November 2015, the auditor testified that it would not be statistically significant to project only two months of sales over the entire 38-month audit period. She also stated that the information provided by the Taxpayer was incomplete.

It is undisputed that the auditor's estimates *could* be higher than the Taxpayer's actual sales amounts and tax liabilities. Of course, the estimates could be lower. As noted, the standard IRS mark-up for the Taxpayer's type of business is 35%. Here, though, the Revenue Department's average mark-up was 24.5%. But the auditor based her estimates on actual numbers from vendor records and the most contemporaneous retail sales

numbers she could determine. And, of course, the estimation was necessitated by the Taxpayer's failure to keep records. "Where there are no proper entries on the records to show the business done, the taxpayer must suffer the penalty of noncompliance and pay on the sales not so accurately recorded as exempt." *State v. T.R. Miller Mill Co.*, 130 So.2d 185, 190 (Ala. 1961). Thus, the Taxpayer has not proven that the estimation of the Taxpayer's sales was in error. *See* Ala. Code § 40-2A-7(b)(5)c.3, stating that a final assessment is presumed correct on appeal and that the Taxpayer bears the burden of proving the assessment incorrect.

The fraud penalty

Ala. Code § 40-2A-11(d) levies a 50-percent penalty for any underpayment of tax due to fraud. The burden of proof in an assessment of a fraud penalty falls on the Revenue Department. Ala. Code § 40-2B-2(k)(7). For purposes of the penalty, "fraud" is given the same meaning as ascribed in the federal fraud provision, 26 U.S.C. §6663. Consequently, federal authority should be followed in determining if the fraud penalty applies. *Best v. State, Dept. of Revenue*, 423 So.2d 859 (Ala. Civ. App. 1982).

The existence of fraud must be determined on a case-by-case basis from a review of the entire record. *Parks v. Commissioner*, 94 T.C. 654, 660 (1990). Because fraud is rarely admitted, "the courts must generally rely on circumstantial evidence." *U.S. v. Walton*, 909 F.2d 915, 926 (6th Cir. 1990). Consequently, fraud may be established from "any conduct, the likely effect of which would be to mislead or conceal." *Id.* The mere underreporting of gross receipts is itself insufficient to establish a finding of fraud, unless there is evidence of repeated understatements in successive periods when coupled with

other circumstances showing an intent to conceal or misstate sales. *Barrigan v. C.I.R.*, 69 F.3d 543 (1995).

A taxpayer's failure to keep adequate books and records, a taxpayer's failure to furnish auditors with records or access to records, the consistent underreporting of tax, and implausible or inconsistent explanations regarding the underreporting are strong indicia of fraud. *See Solomon v. C.I.R.,* 732 F.2d 1459 (1984); *Wade v. C.I.R.*, 185 F.3d 876 (1999). Ignorance is not a defense to fraud where the taxpayer should have reasonably known that its taxes were being grossly underreported. *Russo v. C.I.R.,* T.C. Memo 1975-268; *Temple v. C.I.R.*, 67 T.C. 143 (1976).

The Taxpayer argues that the Revenue Department did not prove that the Taxpayer had a specific intent to evade taxes. He acknowledged in brief, however, that courts generally rely on circumstantial evidence concerning questions of fraud because fraud is rarely admitted, citing *U.S. v. Walton*, 909 F.2d 915, 926 (6th Cir. 1990). "Consequently, fraud may be established from 'any conduct, the likely effect of which would be to mislead or conceal.' *Walton*, 909 F.2d at 926, quoting *Spies v. United States*, 63 S.Ct. 364, 368 (1943). The failure to keep adequate records and the consistent underreporting of tax is strong evidence of fraud." Taxpayer's Post Hearing Brief, 6.

The facts introduced by the Revenue Department clearly show that the Taxpayer's underreporting qualified as fraudulent. The Taxpayer admitted that he kept virtually no records. And the records he kept were either incomplete or showed sales numbers that were less than the wholesale purchase amounts for those corresponding periods (the z-tapes for January, February, and March 2017). Although the Taxpayer collected sales tax

from its customers based on retail selling prices, the Taxpayer treated the tax as operating revenue by using its gross receipts, which included sales tax, to first pay gas suppliers, vendors, employees, and service providers. Only then did the Taxpayer report the net amounts remaining in its checking account as taxable sales. This approach resulted in the Taxpayer reporting total sales of $553,266 during a 38-month period, although it purchased more than $2.7 million of supplies for resale during that same period.

Further, for every month during the audit period, the Taxpayer reported taxable sales to be less than its wholesale purchases, for which the Taxpayer had no plausible explanation. And these figures were not estimated, except for wholesale-purchase amounts from two vendors. The Revenue Department has proven fraud in the Taxpayer's underreporting.

As noted, the Revenue Department's final assessment contains a late-payment penalty in addition to the fraud penalty. However, Ala. Code § 40-2A-11(g) states that, "[i]f the fraud penalty is asserted, no other penalties shall be asserted." Thus, the late-payment penalty must be removed from the Revenue Department's final assessment.

Conclusion

The Revenue Department's final assessment, less the late-payment penalty, is affirmed in the amount of $187,514.64, plus additional interest from the date of the final assessment. Judgment is entered against the Taxpayer accordingly.

The Tax Board's final assessment is affirmed in the amount of $125,090.50, plus additional interest from the date of the final assessment. Judgment is entered against the Taxpayer accordingly.

It is so ordered.

This Opinion and Final Order may be appealed to circuit court within 30 days, pursuant to Ala. Code § 40-2B-2(m).

Entered March 16, 2021.

/s/ *Jeff Patterson*
JEFF PATTERSON
Chief Judge
Alabama Tax Tribunal

jp:cm
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