

K & P ENTERPRISES, INC.	§	STATE OF ALABAMA
D/B/A TOWN MARKET		DEPARTMENT OF REVENUE
8113 OLD HWY 31	§	ADMINISTRATIVE LAW DIVISION
MORRIS, AL 35116-0466,		
	§	
Taxpayer,		DOCKET NO. S. 07-928
	§	
v.		
	§	
STATE OF ALABAMA		
DEPARTMENT OF REVENUE.	§	

**FINAL ORDER**

The Revenue Department assessed K & P Enterprises, Inc. ("Taxpayer"), d/b/a Town Market, for State sales tax for December 2002 through November 2005. The Taxpayer appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on March 14, 2008. CPA Berry Brooks and the Taxpayer's owner, Dalton Chandler, attended the hearing. Assistant Counsel Wade Hope represented the Department.

The Taxpayer operated a combination convenience store/restaurant in a rural area approximately 20 miles northeast of Birmingham, Alabama during the period in issue. The Department audited the Taxpayer for sales tax and requested its sales and other relevant records for December 2002 through November 2005. The Taxpayer's owner provided a few purchase invoices. He failed, however, to provide any cash register z-tapes or other sales records.

The examiner determined that the invoices provided by the Taxpayer were incomplete. He subsequently obtained purchase information from the Taxpayer's vendors. That information showed that the Taxpayer's monthly wholesale purchases greatly exceeded its reported monthly retail sales. The examiner thus concluded that the

Taxpayer's returns were incorrect. He consequently computed the Taxpayer's liability using a purchase mark-up audit.

In conducting the audit, the examiner determined the Taxpayer's wholesale purchases from his vendors' records. He arrived at the Taxpayer's estimated sales by applying the standard 268.94 percent IRS mark-up for restaurants and the 26.79 percent mark-up for convenience stores. He then allowed a credit for tax previously paid by the Taxpayer to arrive at the additional tax due. The Department also applied the 50 percent fraud penalty.

All taxpayers subject to sales tax are required to keep complete and accurate records from which the Department can accurately determine the taxpayer's correct liability. Code of Ala. 1975, §§40-2A-7(a)(1) and 40-23-9; *State v. Mack*, 411 So.2d 799 (Ala. Civ. App. 1982). If a taxpayer fails to keep adequate records, the Department can use any reasonable method to compute the taxpayer's liability. The taxpayer cannot later complain that the liability so computed by the Department is inexact. *Jones v. C.I.R.*, 903 F.3d 1301 (10<sup>th</sup> Cir. 1990).

The Department's use of a purchase mark-up audit is a commonly used and accepted method of computing a taxpayer's sales tax liability in the absence of adequate records. See generally, *Alsedeh v. State of Alabama*, S. 03-549 (Admin. Law Div. 11/3/04); *Arnold v. State of Alabama*, S. 03-1098 (Admin. Law Div. 7/27/04); *Moseley's One Stop, Inc. v. State of Alabama*, S. 03-316 (Admin. Law Div. 7/28/03); *Pelican Pub & Raw Bar, LLC v. State of Alabama*, S. 00-286 (Admin. Law Div. 12/15/00); *Joey C. Moore v. State of Alabama*, S. 99-126 (Admin. Law Div. 8/19/99); *Robert Earl Lee v. State of Alabama*, S. 98-179 (Admin. Law Div. 6/28/99); *Red Brahma Club, Inc. v. State of Alabama*, S. 92-171

(Admin. Law Div. 4/7/95); and *Wrangler Lounge v. State of Alabama*, S. 85-171 (Admin. Law Div. 7/16/86).

The Department examiner determined that the Taxpayer had not correctly reported his monthly sales because his monthly wholesale purchases, without mark-up, greatly exceeded his reported monthly sales. The examiner thus correctly computed the Taxpayer's liability using a purchase mark-up audit.

The Taxpayer's CPA argues that the mark-up percentages used by the examiner were excessive. He also claims that the Taxpayer maintained complete records after the audit, and that the Department should use those post-audit period records to estimate the Taxpayer's liability for the audit period. I disagree.

The mark-up percentages used by the examiner are from a composite mark-up chart used by the IRS. The percentages are reasonable, and the Taxpayer has presented no evidence, other than the owner's unsupported verbal assertions, showing that the percentages are incorrect.

A taxpayer's records for a period other than the period in issue may, under certain limited circumstances, be used to estimate the taxpayer's liability for the period in issue. See generally, *State v. Ludlum*, 384 So.2d 1089 (Ala. Civ. App. 1980). But such records should only be considered if there is no other reasonable method by which a taxpayer's liability for the subject period can be determined.

The Department's mark-up audit was properly performed, and absent evidence to the contrary, represents a reasonable estimate of the Taxpayer's sales during the actual audit period. When a taxpayer fails to keep records that accurately reflect its tax liability for a period, the taxpayer must suffer the consequences. *State v. T. R. Miller Mill Co.*, 130

So.2d 185 (1961). The Department is thereafter entitled to compute the taxpayer's liability by any reasonable method, and the taxpayer cannot thereafter complain that the liability so estimated is incorrect.

In this case, the Taxpayer's post-audit period records should not be used in lieu of the Department's purchase mark-up audit. The examiner used the Taxpayer's actual purchase information from the audit period, and then applied a reasonable mark-up. The sales tax as assessed is due to be affirmed.

The Department added the fraud penalty because the Taxpayer's monthly wholesale purchases exceeded his reported monthly sales. Based on the open and frank testimony and explanations offered by the Taxpayer's owner at the March 14 hearing, the Department agrees, and I concur, that the 5 percent negligence penalty should apply in lieu of the 50 percent fraud penalty.

The tax and interest as assessed by the Department is affirmed. The penalty is reduced to the 5 percent negligence penalty. Judgment is entered against the Taxpayer for tax of \$45,680.80, penalty of \$2,284.04, and interest of \$9,604.17, for a total liability of \$57,569.01. Additional interest is also due from the date the final assessment was entered, September 19, 2007.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered April 1, 2008.

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BILL THOMPSON  
Chief Administrative Law Judge

bt:dr

cc: J. Wade Hope, Esq.  
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