CARLTON L. CLIFTON D/B/A WHISPERING OAKS 707 GENEVA STREET OPELIKA, AL 36801-5808,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Taxpayer,	§	DOCKET NO. S. 08-141
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

OPINION AND PRELIMINARY ORDER

The Revenue Department assessed Carlton L. Clifton ("Taxpayer"), d/b/a Whispering Oaks Bed & Breakfast, for State sales tax for May 2003 through April 2006. 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 June 12, 2008. The Taxpayer attended the hearing. Assistant Counsel Wade Hope represented the Department.

The Taxpayer operated restaurants in Opelika and Tuskegee, Alabama during the period in issue. He closed the Tuskegee business and opened another restaurant in Auburn, Alabama in January 2006.

The Department audited the Taxpayer for State sales tax for the subject period. It requested records from which the Taxpayer's sales tax liability could be computed. The Taxpayer provided some bank records, purchase invoices, cash receipts, and copies of various income tax returns. He failed, however, to provide any cash register tapes or other complete sales records.

The Department examiners reviewed the Taxpayer's records and determined that he had underreported his taxable sales during the audit period. Because the Taxpayer's sales records were incomplete and otherwise insufficient, the examiners computed the

Taxpayer's liability using a purchase mark-up audit.

The examiners determined the Taxpayer's wholesale purchases using his canceled checks, cash paid receipts, and vendor records. They estimated that 25 percent of the Taxpayer's purchases from Wal Mart and Sam's Club were for nontaxable supplies. They consequently removed those amounts from the audit. They then applied a 2.50 percent mark-up to arrive at the Taxpayer's total sales. The examiners' audit report explains that the standard IRS mark-up for restaurants is 2.695 percent, but that the lower mark-up "was used for buffet business considerations and family use of the restaurant." State Ex. 2 at 5. After computing the total tax due, the examiners allowed a credit for tax paid to arrive at the additional tax due.

The Taxpayer explained at the June 12 hearing that the Department had previously audited and assessed him for sales tax for July 2000 through April 2003. He also appealed that final assessment to the Administrative Law Division. The Administrative Law Division affirmed the tax and interest due, less the penalties, primarily because the Taxpayer had failed to keep records properly documenting his exempt sales during the period. See, *Clifton v. State of Alabama*, S. 04-299 (Admin. Law Div. 10/27/2004).

The Taxpayer argues in this case that he kept records showing his exempt sales. He also claims that the Department audit ignores the fact that he sometimes reduced his prices to stimulate business. For example, he offered a co-worker discount where one person would pay full price and a co-worker could eat for free. He also had a senior citizen discount. The Taxpayer also claims that when he sold meals to the City of Opelika that were used to feed inmates in the Opelika jail, he only made a few cents on each meal, and

not the large mark-up applied by the Department.

The Department contends that it removed all sales from the audit if the Taxpayer provided records showing that the sale was to or paid for by an exempt entity. The Taxpayer submitted a number of credit card receipts that he claims were paid by the National Guard or another exempt entity. As indicated, the Department deleted any sales if a receipt showed the Guard or another exempt entity as the purchaser. Unfortunately, a number of the receipts were faded and could not be read. The Department did not remove those sales from the audit.

The Department also reduced the Taxpayer's monthly sales to reflect the reduced price he charged for the inmate meals. For example, the Department subtracted $6,500, $6,100, and $4,700 from the Taxpayer's sales in the last three months of the audit period, respectively, to reflect the reduced inmate meal prices. It contends that even if the sales to the City of Opelika were removed entirely, the mark-up percentage would still be 2.23 percent.

The Taxpayer's prior appeal before the Administrative Law Division also involved sales that the Taxpayer claimed were to the National Guard and other exempt entities. The Final Order entered in the case reads in pertinent part as follows:

> The Taxpayer argues that the meals in question were exempt from sales tax because they were made to either the City of Tuskegee, the City of Opelika, or the State or U.S. Government. He explained that Opelika and Tuskegee officials routinely asked him to provide meals to transients, homeless people, and others in need of temporary assistance. However, the Cities never issued purchase orders to the Taxpayer, and the meals were paid for by various churches and other charitable and nonprofit groups in the area.
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> The Taxpayer also contends that some of the meals in issue were sold to the Army Reserve or the National Guard. He explained that the Reserve or

> Guard would call him and request that he provide meals for Reserve or Guard members. He would provide the meals and, according to the Taxpayer, the Reserve or Guard would then pay for the meals by giving him a government credit card number over the telephone. Again, there is no documentation that the meals were ordered or paid for by the Reserve or Guard.
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> Based on the Taxpayer's testimony, it appears that the City of Tuskegee and the City of Opelika may have arranged and coordinated the Taxpayer's providing of the meals to the various needy individuals. However, to qualify as an exempt sale, the Taxpayer was required to obtain a purchase order from the exempt City, and the City must have actually paid for the meals with City funds. Dept. Reg. 810-6-3-.69.02.
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> There are no purchase orders or other tangible evidence that the City of Tuskegee or the City of Opelika ordered the meals from the Taxpayer. The meals were also paid for by various churches and charities in the area, not the Cities. While churches and charities are worthwhile organizations that perform many good deeds, there is no blanket exemption from sales tax for all churches and charities. The Alabama Legislature has specifically exempted many charities and other organizations from tax. (footnote omitted) However, none of those exempt organizations purchased the meals in issue.
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> Even if the sales had been to the Cities, the Taxpayer failed to properly document the sales. He failed to provide purchase orders from the Cities concerning the sales, and, as indicated, there is no tangible evidence that the Cities paid for the meals that were included in the audit. (footnote omitted) The burden is on a taxpayer to document all exempt sales, and if a taxpayer fails to properly maintain adequate records, the taxpayer must suffer the consequences and pay sales tax on those sales not accurately recorded as exempt. *State v. Ludlum*, 384 So.2d 1089 (Ala. Civ. App.) *cert. denied*, 384 So.2d 1094 (Ala. 1980).
>
> The above rationale also applies to the sales the Taxpayer claims he made to the Army Reserve and the National Guard. There is no tangible evidence that the Reserve or the Guard ordered the meals, or that they paid for the meals. Without such records, no exemption can be allowed.

Clifton, *supra* at 1 – 3.

As in the prior appeal, the problem in the current case is that the Taxpayer failed to keep his cash register tapes or any other accurate sales records. The Taxpayer contends

that he kept good records because he maintained a daily "fact sheet" at the restaurants. But as indicated, he failed to maintain the underlying cash register tapes and/or sales tickets on which the fact sheet totals are based.

All taxpayers subject to sales tax are required to keep contemporaneous sales records from which the Department can accurately compute and verify the taxpayer's liablity. "The State is not required to rely on verbal assertions of the taxpayer in determining the correctness of the tax return, but records should be available disclosing the business transacted. Where there are no proper entries on the records . . . , the taxpayer must suffer the penalty of noncompliance and pay on the sales not so accurately records as exempt." *State v. Ludlam*, 384 So.2d 1089, 1091 (Ala. Civ. App.) *cert. denied*, 384 So.2d 1094 (Ala. 1980), quoting *State v. T. R. Miller Mill Co.*, 130 So.2d 185 (1961).

The Taxpayer asserts that even if he had kept his cash register tapes, the tapes would not show if a particular sale was to an exempt entity. That is correct, but the Taxpayer's total sales could be verified by those tapes. To verify an exempt sale, the Taxpayer must provide a purchase invoice issued by the exempt entity and/or a sales ticket or invoice made out to the exempt entity, and also proof that the meal or meals were paid for by the exempt entity. The Taxpayer should also maintain all of his purchase invoices, and, importantly, all of his cash register tapes. It cannot be presumed that a sale is exempt, and without proof that a sales was to an exempt entity, the sale must be treated as taxable. The Taxpayer also may have sold some meals at a reduced price, but without accurate and complete sales records, that claim cannot be verified.

Giving the Taxpayer the benefit of the doubt, the Department should recompute his liability using the reduced 2.23 percent mark-up. It should then notify the Administrative Law Division of the adjusted amount due. An appropriate Final Order will then be entered.

This Opinion and Preliminary Order is not an appealable Order. The Final Order, when entered, may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered August 13, 2008.

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BILL THOMPSON
Chief Administrative Law Judge

bt:dr
cc: J. Wade Hope, Esq.
Carlton Clifton
Joe Cowen
Mike Emfinger