

SUBHANSH, INC  
d/b/a SHOPPER STOP 37  
2225 MARVYN PKWY.  
OPELIKA, AL 36804,

Taxpayer,

v.

STATE OF ALABAMA  
DEPARTMENT OF REVENUE.

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STATE OF ALABAMA  
DEPARTMENT OF REVENUE  
ADMINISTRATIVE LAW DIVISION

DOCKET NO. S. 13-268

### FINAL ORDER

The Revenue Department assessed Subhansh, Inc., d/b/a Shopper Stop 37 (“Taxpayer”), for State sales tax for January 2006 through April 2011. 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 May 9, 2013. Sanjay Patel represented the Taxpayer. Assistant Counsel Margaret McNeill represented the Department.

The Taxpayer operated a convenience store/deli in Opelika, Alabama during the period in issue.

The Department audited the Taxpayer for the period and requested all of the Taxpayer’s sales tax-related records. The Taxpayer provided a sales journal, some purchase invoices, bank statements, and income tax returns. The Taxpayer’s owner told the examiner that he entered his daily sales totals into the sales journal. He then sent the monthly total to his accountant, who electronically filed the Taxpayer’s monthly returns. Unfortunately, the Taxpayer failed to provide any cash register z-tapes that verified the monthly sales journal amounts.

Because the Taxpayer failed to provide any z-tapes, the examiner reviewed the Taxpayer’s bank statements and other records to determine if it had accurately reported its

sales during the period. The examiner's audit report reads in part as follows:

The business bank statements were analyzed, and a bank deposit analysis summary was scheduled to determine if there were any excess deposits over reported sales. There were three business accounts, the main account, the gas account and a Western Union account. All deposits for each account were analyzed and adjustments were made to remove gasoline sales, transfers between accounts, returned deposit items, rebates (from tobacco companies), Western Union payments and transfers, money orders, and tax collected. Cash payouts were added back to the deposits because the money was taken from the registers and never deposited into the bank account. These amounts were arrived at taking the purchase invoices and statements received from the vendors and comparing it to the checks written. The adjusted amounts of deposits were compared to the amount of taxable sales reported each month. The deposit analysis was not in line with sales reported; therefore, I continued to verify purchase information.

All purchase invoices of resale merchandise were sorted and totaled by vendor for the audit period. These figures were then used to determine the total amount of purchases made on a monthly basis. Not all of the purchase invoices were received; therefore, third parties were contacted. After receiving third party information, the purchases were compared to the monthly sales reported. The total purchases scheduled for the audit period were \$2,127,896.88 and the sales reported were \$1,883,232.52; which is significantly lower than the purchases. Since purchases exceeded sales reported, an indirect audit method of a purchase markup audit was used to determine the total tax due.

The examiner conducted the purchase mark-up audit by first listing the Taxpayer's total purchases per the Taxpayer's purchase invoices and additional vendor records. She then determined the mark-up for the cigarettes and other tobacco products, beer and wine, groceries, and miscellaneous items by taking various samples of each of those type items in the Taxpayer's store and comparing the actual selling prices to the Taxpayer's wholesale costs of the items. The resulting mark-ups were 12.67%, 22.67%, 56.13%, and 11.45%, respectively. She also used the IRS statistical mark-up of 83.17% for eating and drinking places as the mark-up for the deli items.

The examiner applied the above mark-ups to the Taxpayer's purchases to determine the total tax due. She then allowed a credit for sales tax reported and paid during the period to arrive at the additional tax due. The 5% negligence penalty was also assessed because the Taxpayer had failed to keep complete and accurate records during the period.

All retailers subject to Alabama sales tax are statutorily required to keep complete accurate sales, purchase, and other records from which their correct sales tax liability can be computed. Code of Ala. 1975, §§40-2A-7(a)(1) and 40-23-9. A retailer's duty to keep sales records is straightforward and simple. The retailer must record all sales on a cash register z-tape and/or on customer invoices or receipts, which may then be compiled onto a monthly sales journal. It is commonly understood that such records must be maintained to allow the Department to verify that the correct amount of sales tax has been reported and paid.

The Taxpayer in this case failed to provide any cash register z-tapes. In such cases, the Department is authorized to compute a taxpayer's correct liability using the most accurate and complete information obtainable. Code of Ala. 1975, §40-2A-7(b)(1)a. The Department can also use any reasonable method to compute the liability, and the taxpayer, having failed in the duty to keep good records, cannot later complain that the records and/or method used by the Department is improper or does not reach a correct result. *Jones v. CIR*, 903 F.3d 1301 (10th Cir. 1990); *State v. Ludlum*, 384 So.2d 1089 (Ala. Civ. App.), cert. denied, 384 So.2d 1094 (Ala. 1980) (A taxpayer must keep records showing the business transacted, and if the taxpayer fails to keep such records, the taxpayer must

suffer the penalty for noncompliance). The Department examiner thus properly conducted a purchase mark-up audit to compute the Taxpayer's liability for the subject period.

The purchase mark-up audit is a simple, oft-used Department method of determining a taxpayer's sales tax liability when the taxpayer fails to keep accurate sales records. See generally, *GHF, Inc. v. State of Alabama*, S. 09-1221 (Admin. Law Div. 8/10/10); *Thomas v. State of Alabama*, S. 10-217 (Admin. Law Div. O.P.O. 5/18/10); *Alsedeh v. State of Alabama*, S. 03-549 (Admin. Law Div. 11/3/04).

The Taxpayer's owner argued at the May 9 hearing that he did not know that sales tax was owed on telephone card sales, and that he consequently did not collect sales tax on those sales. He also asserted that his mark-ups on beer and cigarettes were lower than the mark-up percentages used by the examiner in her audit. He reiterated those claims in a post-hearing letter to the Administrative Law Division.

The Taxpayer appears to be a sincere individual, but the fact that he was not aware that sales tax was owed on phone cards does not change the fact that he owes tax on the cards that he sold during the audit period. The owner may also be correct that the mark-up percentages used by the examiner for beer and cigarettes was too high, but the mark-ups were determined using the actual prices the examiner took from a sampling of the items in the Taxpayer's store. Importantly, if the owner had maintained complete and accurate cash register tapes, there would have been no need for the examiner to compute the mark-ups.

The evidence also establishes that the Taxpayer had substantially underreported its sales during the audit period. For a retail business to continue operating, it must sell its

merchandise for a price sufficient to buy the merchandise from the wholesaler, and to also pay all operating costs, i.e., labor costs, utilities, rent or mortgage costs, business and other licenses and taxes, etc. In this case, however, the total sales reported by the Taxpayer for the audit period (\$1,883,232.52) were considerably less than the cost of the goods sold (\$2,127,896.88). The only conclusion is that the Taxpayer underreported its taxable sales during the period. I also note that in similar cases the Department has assessed, and the Administrative Law Division has affirmed, the 50 percent fraud penalty, not the 5 percent negligence penalty that was assessed in this case. See generally, *Ashland Enterprises v. State of Alabama*, Docket S. 12-236 (Admin. Law Div. 1/16/2013); *Melton v. State of Alabama*, Docket S. 10-376 (Admin. Law Div. 11/4/2010).

The final assessment is affirmed. Judgment is entered against the Taxpayer for State sales tax, penalty, and interest of \$79,101.92. Additional interest is also due from the date the final assessment was entered, February 1, 2013.

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

Entered June 10, 2013.

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BILL THOMPSON  
Chief Administrative Law Judge

bt:dr

cc: Margaret Johnson McNeill, Esq.  
Sanjay R. Patel  
Joe Walls  
Mike Emfinger