ALABAMA TAX TRIBUNAL

CRESVIEW FOODS, LLC, AND ITS SOLE MEMBER, AHMED DHARANI,	§	
Taxpayer,	§	DOCKET NO. S. 20-759-JP
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

OPINION AND FINAL ORDER

This appeal involves a final assessment of state sales tax for January 2017 through May 2019. A trial was held on December 8, 2022. Stephen H. Schniper represented the Taxpayer, and Ahmed Dharani appeared and testified. Margaret McNeill represented the Revenue Department. William Jamar, a Revenue Department supervisor, appeared and testified. Justin Zehnder and Elizabeth LeCroy appeared under subpoena at the request of the Taxpayer. The parties were given an opportunity after the trial to discuss possible adjustments to the final assessment or a settlement of the case; however, the parties were unable to reach an agreement.

Facts

Since 2008, Cresview Foods, LLC, operated as a convenience store in Dora, Alabama. Ms. LeCroy testified that, when she conducted the audit of the Taxpayer, Mr. Dharani informed her that he had no cash register z-tapes from the audit period. However, he provided point-of-sale monthly summaries from one of the store's three cash registers for one year of the 29-month audit period, and she also examined

vendor invoices and grocery items.

Ms. LeCroy testified that the amount of the Taxpayer's wholesale purchases from vendors during the audit period was $3,447,026.19. According to Mr. Jamar, the total amount of retail sales reported by the Taxpayer on its sales tax returns for the audit period was $3,234,833.99. Therefore, wholesale purchases exceeded the amount of reported taxable sales by more than $200,000. In fact, purchases exceeded sales for most months. Therefore, Ms. LeCroy did a purchase markup audit using a 35% markup, which resulted in a total estimated taxable measure of $4,581,440.89 over the 29 months under audit.

Ms. LeCroy testified that she completed a shelf test on the Taxpayer's store using retail prices provided by the store's clerk and wholesale prices provided by Mr. Dharani. The test involved a comparison of the wholesale prices paid by the Taxpayer for certain items with the retail prices of those same items as evidenced by the prices charged in the Taxpayer's store. According to Ms. LeCroy, the shelf test showed that the Taxpayer's actual purchase markup was 39%. She gave the Taxpayer credit for beginning and ending inventory so that those items would not be counted as having been sold and would not be subject to mark-up. Also, Ms. LeCroy testified that the Wholesale to Retail Accountability Program ("WRAP") data she received was attributable to the Taxpayer because it included the Taxpayer's name, sale tax number, and the location of the store.

According to Ms. LeCroy, the fraud penalty was assessed because the Taxpayer's purchases during the audit period exceeded reported taxable sales.

According to Ms. LeCroy, the fact that a business's purchases would exceed sales over a 29-month period is not sustainable. She also testified that the Taxpayer had received two WRAP inquiry letters because its purchases had exceeded reported taxable sales during two previous quarters, thus triggering the Revenue Department's audit.

Mr. Jamar testified that the fraud penalty was assessed because sales were admittedly underreported, with no justification. Also, the Taxpayer did not maintain daily z-tapes for the audit period. According to Mr. Jamar, even if Mr. Dharani had been lending the Taxpayer money to operate, as claimed, that fact would not explain the discrepancy between purchases and reported sales.

Mr. Dharani testified that he has been in business in Alabama since 2008 and that he currently operates four stores and a software company. He testified that he had three registers in the convenience store in issue, one of which was used for gas purchases. He stated that he provided monthly summaries of z-tapes to the auditor for two of the cash registers for a one-year period, but that the daily z-tapes had been reused and printed over in the registers. The third register's sales were recorded on a daily report and were manually entered into the Taxpayer's point-of-sale system. Mr. Dharani testified that he provided the Revenue Department with invoices from all vendors for grocery items, as well as checks for 2017 and 2018 and bank statements.

With respect to the items listed on the shelf test, Mr. Dharani stated that he barely sold some of the items listed and that the items included on the list have a

higher markup. He testified that 53% of his purchases were cigarettes and that his markup on cigarettes is 9%. He also testified that beer and liquor comprise 30% of his purchases. According to Mr. Dharani, the remainder of his sales are grocery and breakfast items. He testified that a 20-ounce soda is his best seller and that the markup on one soda is 66%, but that the markup when a customer buys two sodas is 38%.

Mr. Dharani also stated that he provided a police report to the auditor showing theft in his store, although he did not produce a report at trial. According to Mr. Jamar, however, theft is factored into the 35% markup used by the Revenue Department.

Mr. Dharani acknowledged that he underreported his sales but disagrees with the Revenue Department's markup percentage. In summary, he believes that the Revenue Department "cherry-picked" items for the shelf test which generated a higher markup percentage. Ms. LeCroy stated, however, that she did not do so. Instead, she stated that she based her audit on the amount of the Taxpayer's purchases and the amount of reported sales, which are actual numbers and not estimates.

Discussion

On appeal, the Taxpayer challenges the 35% purchase markup and the assessment of the fraud penalty.

Assessment of Tax

The Taxpayer failed to maintain complete sales records. When a Taxpayer fails to do so, the Revenue Department may compute the Taxpayer's tax liability "using the most accurate and complete information obtainable." Jai Shanidev Inc. d/b/a Country Corner, S. 16-449 (Ala. Tax Tribunal 04/27/17); Ala. Code 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 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)."

Jai Shanidev Inc. d/b/a Country Corner, supra.

Because the Taxpayer here failed to maintain complete sales records for the audit period, the Revenue Department conducted a purchase markup audit of the Taxpayer and applied a markup of 35% to the Taxpayer's purchases. As the Tax Tribunal has explained in previous cases, the 35% purchase markup is based on Internal Revenue Service information regarding percentage markups of gas stations and grocery stores. The percentages have been averaged to reach the 35% figure.

See, e.g., E&Z, Inc. v. State of Ala. Dep't of Rev., S. 19-989-LP (Ala. Tax Tribunal 1/12/2022). The Tribunal has previously held that that percentage is reasonable. See, e.g., E&Z, Inc., supra.

Section 40-2A-7(b)(5)c.3, Ala. Code 1975, states the following: "On appeal … to the Alabama Tax Tribunal, the final assessment shall be prima facie correct, and the burden of proof shall be on the taxpayer to prove the assessment is incorrect." Although the Taxpayer argued that the 35% markup was improper, the Taxpayer did not offer documentary proof that the estimated percentage markup was higher than the Taxpayer's actual markup. Instead, Ms. LeCroy testified that the shelf test that she conducted indicated that the Taxpayer's markup was 39%, which was higher than the markup applied by the Revenue Department. Therefore, the Taxpayer has failed to meet its burden of showing that the tax component of the final assessment is incorrect. That portion of the final assessment is upheld.

Assessment of the Fraud Penalty

The Taxpayer next challenges the assessment of the fraud penalty. The Tax Tribunal has previously explained:

> "Ala. Code § 40-2A-11(d) levies a 50 percent fraud penalty for any underpayment of tax due to fraud. The burden of [persuasion] in an assessment of a fraud penalty falls on the 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 under-reporting 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.00R., T.C. Memo 1975-268; Temple v. C.I.R., 67 T.C. 143 (1976)."
>
> "Any retailer should know with certainty that sales records must be maintained for audit purposes…."

E&Z, Inc., v. State of Alabama Department of Revenue, 19-989-LP (Ala. Tax Tribunal 1/12/22).

In this case, Revenue Department personnel testified that the fraud penalty was assessed because the Taxpayer's reported sales were $200,000 less than the Taxpayer's wholesale purchases during the audit period and because the Taxpayer did not maintain daily sales information that would have established actual sales amounts. If the Taxpayer's markup had been only 20%, as the Taxpayer stated was customary for convenience stores, then its reported sales would have been slightly more than $4 million ($3.4 million in purchases increased by 20%) for the audit period). Instead, the Taxpayer actually reported only $3.2 million in taxable sales for

that period. Therefore, the Revenue Department's assessment of the fraud penalty is upheld.

Conclusion

Based on the foregoing, the Revenue Department's final assessment is upheld. Judgment is entered against the Taxpayer and in favor of the Revenue Department in the amount of $87,265.51, plus additional interest that continues to accrue from the date of entry of the final assessment until the liability is paid in full.

It is so ordered.

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

Entered May 5, 2023.

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

jp:ac
cc: Stephen H. Schniper
Ahmed Dharani
Margaret Johnson McNeill, Esq.