

COMMONWEALTH OF MASSACHUSETTS

APPELLATE TAX BOARD

CHAN MARKET, INC.¹

v.

COMMISSIONER OF REVENUE

Docket No. C311903

Promulgated:
December 5, 2013

This is an appeal filed under the formal procedure pursuant to G.L. c. 58A, § 7 and G.L. c. 62C, § 39, from the refusal of the Commissioner of Revenue ("Commissioner" or "appellee") to abate sales taxes for the quarterly periods ended September 30, 2006 through June 30, 2009 ("periods at issue"),² assessed to Chan Market, Inc. ("appellant"), under G.L. c. 64C and G.L. c. 64H, as well as underpayment penalties assessed under G.L. c. 62C, § 35A.

Commissioner Chmielinski heard the appeal. Chairman Hammond, Commissioners Scharaffa, Rose, and former Commissioner Mulhern joined him in the decision for the appellee.

These findings of fact and report are issued pursuant to a request by the appellee under G.L. c. 58A, § 13 and 831 CMR 1.32.

¹ The Petition relating to this appeal identified Mr. Heip Tran, the president of Chan Market, Inc., as the appellant. However, the disputed assessment was issued to Chan Market, Inc., which was also the entity on behalf of which the relevant Application for Abatement was filed.

² The assessment did not include the quarterly period ended December 31, 2008, for which the appellant filed a delinquent return consistent with the Commissioner's calculation of the appellant's outstanding sales tax liability.

Heip Tran, pro se, for the appellant.

Timothy R. Stille, Esq. for the appellee.

FINDINGS OF FACT AND REPORT

Based on testimony and exhibits entered into evidence at the hearing of this appeal, the Appellate Tax Board ("Board") made the following findings of fact.

At all times relevant to the appeal, the appellant owned and operated a liquor store located in Roslindale, Massachusetts. During April of 2009, the Commissioner initiated an audit of the appellant. As a result of the audit, the Commissioner issued a Notice of Intent to Assess sales/use tax dated July 31, 2010, in the amount of \$16,958.11, inclusive of interest and penalties. The Commissioner subsequently issued a Notice of Assessment dated September 8, 2010, in the amount of \$17,046.46, which reflected the accrual of additional interest. The appellant filed an Application for Abatement on November 9, 2010, which the Commissioner denied on April 12, 2011.³ The appellant filed its Petition Under Formal Procedure with

³ The appellant also filed an Application for Abatement on November 9, 2010 concerning an assessment for excise on cigars issued by the Commissioner pursuant to G.L. c. 64C for several of the quarterly periods at issue. The petition relating to the present appeal, however, made no reference to the assessment. Nor did the appellant contest the imposition of the cigar excise during the course of this appeal. Consequently, these Findings do not address the Commissioner's cigar excise calculations, which were used to derive a portion of the assessment at issue in this appeal.

the Board on May 27, 2011. On the basis of these facts, the Board found and ruled that it had jurisdiction to hear and decide the appeal.

Prior to the commencement of the audit giving rise to the present appeal, Ms. Mary Ann Guay, an auditor employed by the Massachusetts Department of Revenue, identified substantial discrepancies between the appellant's wholesale purchases of cigarettes for the periods at issue, as reflected in data provided by a cigarette wholesaler, and taxable retail sales reported by the appellant on Forms ST-9Q, Quarterly Sales and Use Tax Returns, ("Forms ST-9Q"). More specifically, for the quarterly periods ended September 30, 2006 through September 30, 2008, the appellant reported taxable retail sales of cigarettes on Forms ST-9Q ranging from approximately \$5,150 to \$5,800. In contrast, the sum of the appellant's wholesale cigarette purchases for each of these quarterly periods, which is not in dispute, was roughly four times the total of its reported taxable retail sales.⁴ Based on this disparity, the Commissioner initiated an audit and Ms. Guay made several unsuccessful

⁴ For the quarterly periods ended March 31, 2009 and June 30, 2009, the appellant reported taxable retail sales that roughly comport with its wholesale cigarette purchases. This dramatic change coincided with enactment of G.L. c. 64H, § 3A, which requires prepayment of sales tax on tobacco products by those engaged in the retail sale of those products. Effective September 1, 2008, tobacco retailers such as the appellant prepaid sales tax on the wholesale price of tobacco products, collected and remitted sales tax on their retail sales of the products, and claimed a credit for the prepaid tax on their sales tax returns. *Id.*

attempts to meet with Mr. George Johnson, then the appellant's accountant. Ultimately, Ms. Guay met with Mr. Tran on several occasions during the audit.

Soon after the audit commenced, Ms. Guay learned from Mr. Tran that the appellant retained virtually no record of taxable retail sales. In particular, the appellant used a single register key to ring in all sales, taxable or otherwise. Further, the appellant did not retain any register tapes, maintain a daily sales journal, or track inventory. Finally, when asked during the audit what percentage mark-up had been applied to the wholesale cost of cigarettes during the periods at issue, Mr. Tran replied that the mark-up changed every quarter. Given these facts, and in light of the glaring disparity between reported taxable retail sales and wholesale cigarette purchases for the majority of the periods at issue, Ms. Guay concluded that the appellant's records were not adequate to establish its taxable retail sales.

To arrive at taxable retail sales, Ms. Guay produced a summary of the appellant's cigarette purchases to which she applied a mark-up of twenty-five percent, consistent with the presumptive minimum mark-up provided by G.L. c. 64, § 13. She applied the same mark-up to the appellant's wholesale cigar purchases, the sum of which the appellant does not dispute and which were gleaned from wholesaler data and the appellant's

invoices. Ms. Guay then calculated the appellant's sales tax liability by multiplying taxable sales by the statutorily mandated tax rate, allowing a credit for taxes paid by the appellant during the periods at issue.⁵ For each of the quarterly periods ending September 30, 2006 through September 30, 2008, the resultant liability exceeded the appellant's reported liability by more than one thousand dollars and a minimum of approximately 250% to more than 600%. Based on these facts and the totality of the circumstances, the Commissioner assessed so-called "substantial underpayment penalties" pursuant to G.L. c. 62C, § 35A ("§ 35A") for these quarterly periods.

Mr. Tran, the appellant's sole witness, testified regarding the appellant's business and filing practices during the periods at issue. Mr. Tran asserted that he, on behalf of the appellant, had always acted in good faith with respect to the appellant's sales tax filings, and placed unspecified blame for the appellant's filing shortcomings on two former accountants, the first of whom, Robert Moynihan, became ill and passed away during 2007. Mr. Tran stated that the computer of the appellant's second accountant, George Johnson, had "crashed," presumably limiting access to records and impeding the appellant's ability to file proper returns. Mr. Tran, however,

⁵ The assessment also included tax on sales of miscellaneous items sold at the appellant's store, which comprised a negligible fraction of the appellant's liability. The appellant did not contest this portion of the assessment.

presented no evidence whatsoever, beyond his own self-serving statements, to corroborate his assertion that the actions of either accountant had any effect on the appellant's tax filings for any of the periods at issue.

The appellant, through the testimony of Mr. Tran, focused almost exclusively on its retail sales of cigarettes, which accounted for approximately ninety-six percent of the assessment. The appellant did not assert that there was a material difference between wholesale cigarette purchases calculated by the Commissioner and wholesale purchases the appellant ultimately acknowledged making, or that those cigarettes had not been sold at retail by the appellant. Rather, Mr. Tran testified that throughout the periods at issue, the appellant sold cigarettes at a five percent mark-up over their wholesale invoice cost rather than the twenty-five percent mark-up employed by the Commissioner. Implicitly acknowledging that sales had been grossly underreported from June 1, 2006 to September 30, 2008, Mr. Tran asserted that the appellant's liability should equal 105% of the appellant's wholesale cigarette purchases for the periods at issue and submitted a chart illustrating his calculations.⁶ Mr. Tran made no specific

⁶ Mr. Tran's calculations, presumably by mistake, failed to account for his stated mark-up in arriving at the appellant's claimed liability. Instead, Mr. Tran applied the sales tax to the wholesale invoice cost of the cigarettes. Further, the calculations made no provision for the sale of cigars.

argument with respect to retail sales of cigars as determined by the Commissioner.

The appellant also sought abatement of the § 35A penalties. The sole arguments offered in support of the penalty abatement were the appellant's claimed good faith efforts toward tax compliance during the periods at issue and its assertion of a consistent five percent mark-up on cigarettes.

The Board found that Mr. Tran's testimony, and in turn the appellant's claims, lacked credibility. From the beginning of the periods at issue until prepaid tax was incorporated in the wholesale cigarette price, the appellant reported retail sales and remitted tax on a fraction of what Mr. Tran now admits were its wholesale purchases and retail sales of cigarettes. This practice changed abruptly when the appellant's receipt of credit for prepaid sales tax required declaration of at least the purchase price of cigarettes on Forms ST-9Q. Further, Mr. Tran provided no documentation whatsoever - with the exception of self-serving, recently-prepared calculations - to support his assertion that the appellant's outstanding sales tax liability was far less than that calculated by the Commissioner. Indeed, Mr. Tran's assertion of an unchanging five percent mark-up on cigarettes stands in stark contrast with his statement during the audit that the appellant's mark-up on cigarettes varied from quarter to quarter. Moreover, Mr. Tran acknowledged the dearth

of records of taxable retail sales as well as business practices which precluded the ability to confirm those sales, including: use of a single register key to ring in all sales; failure to retain register tapes; failure to maintain a daily sales journal; and failure to track inventory.

In sum, on the basis of the evidence presented and for the reasons discussed further in the Opinion below, the Board found and ruled that the appellant failed to meet its burden of proving its entitlement to abatement of sales taxes or § 35A penalties for the periods at issue. Accordingly, the Board issued a decision for the appellee in this appeal.

OPINION

Sales Tax

In addition to the excise applicable to the sale of tobacco products pursuant to G.L. c. 64C, Massachusetts imposes sales tax on the retail sale of those products, which include cigarettes and cigars. See G.L. c. 64H. The dispute in this appeal centers not on whether the appellant bore a sales tax liability from its sales of cigarettes and cigars during the periods at issue in excess of that reported on its Forms ST-9Q, but the amount of that liability.

The appellant's calculation of its liability hinges entirely on its naked assertion that cigarettes were sold at a mark-up of five percent over wholesale invoice cost throughout the periods at issue. The evidence presented, however, did nothing to support this assertion. To the contrary, the evidence showed gross underreporting of retail sales, inconsistent statements made by Mr. Tran regarding the appellant's mark-up on cigarettes, woefully inadequate recordkeeping, and business practices that provided no basis to establish taxable retail sales. Having found that Mr. Tran's testimony, which comprised almost the appellant's entire case, lacked credibility, the Board gave no weight to the appellant's calculation of its sales tax liability.

On the other hand, the methodology employed by the Commissioner to estimate the appellant's taxable sales was based on essentially undisputed wholesale purchases. In light of the lack of records substantiating the appellant's retail sales of cigarettes, the Commissioner applied the presumptive minimum mark-up to the appellant's wholesale invoice cost pursuant to G.L. c. 64, § 13. Section 13 provides that cigarettes are generally to be sold at a minimum price equal to their "presumptive cost" to a retailer, which is calculated by adding a retailer's "cost of doing business" to its invoice cost.

G.L. c. 64C, § 13(b).⁷ The statute includes a rebuttable presumption that a retailer's cost of doing business is twenty-five percent of its invoice cost and hence a presumptive minimum mark-up of the same amount. **Id.** The appellant's claim that it sold cigarettes at prices far below its presumptive costs, to which the Board afforded no weight, did nothing to rebut application of the presumptive minimum mark-up. The Commissioner also applied a twenty-five percent mark-up to the appellant's purchases of cigars, which the appellant did not substantively challenge. In sum, the appellant provided no credible evidence to undermine the validity of the Commissioner's ostensibly sound audit methodology.

Underpayment Penalty

The underpayment penalty provided by § 35A applies only in cases where a return has been filed. See G.L. c. 62C, § 35A. The underpayment of tax must be attributable to "negligence or disregard" of the tax laws of the Commonwealth, or of public written statements issued by the Commissioner, or to a "substantial understatement" of liability. **Id.** Consistent with the provisions of § 35A, the Commissioner has stated that "negligence" includes "a taxpayer's failure to make a reasonable

⁷ This appeal addresses only at what price the appellant sold cigarettes, not whether and under what circumstances a taxpayer may sell cigarettes for less than the presumptive minimum cost. See generally, **Duarte v. Commissioner**, Mass. ATB Findings of Fact and Reports 2006-490, *aff'd in part*, 451 Mass. 399 (2008).

attempt to comply with the laws or the Commissioner's public written statements" and "disregard" includes any "careless, reckless, or intentional disregard of the laws or public written statements." **Technical Information Release 06-5.** "An understatement is substantial for any tax period if it exceeds the greater of 10% of the tax required to be shown on the return or \$1,000." **Id.**

The appellant's argument that the penalties imposed pursuant to § 35A should be abated was predicated on its assertions that it consistently acted in good faith to comply with its sales tax filing and payment obligations and that cigarettes were sold at five percent above cost throughout the periods at issue. The appellant's assertions, however, stand in sharp contrast with the evidence of record, which indicates that all of the criteria relevant to imposition of the § 35A penalty were present in this case. First, the appellant's returns reflect a substantial understatement of liability within the meaning of § 35A as the appellant reported a mere fraction of taxable retail sales for the quarterly periods to which the penalty was applied and the appellant's ultimate liability exceeded its reported liability by more than one thousand dollars for each of those quarterly periods. Further, the appellant offered nothing but self-serving testimony to dispel the inference that its filing activities were neither negligent

nor in disregard of the Commonwealth's tax laws. In fact, the appellant's activities, evidenced in large measure by the dramatic rise in its reported taxable sales after incorporation of sales tax in the wholesale cost of cigarettes, point to the opposite conclusion. As such, the Board could discern no reason to abate the § 35A penalties.

The appellant bears the burden of proving its right as a matter of law to an abatement. See *M & T Charters, Inc. v. Commissioner of Revenue*, 404 Mass. 137, 140 (1989); *Stone v. State Tax Commission*, 363 Mass. 64, 65-66 (1973); *Staples v. Commissioner of Corps. and Taxation*, 305 Mass. 20, 26 (1940). When a taxpayer challenges an assessment made by the Commissioner, "[t]he burden is on the taxpayer to show error in the assessment and impropriety in the method used." *Allied Building Credits, Inc. v. State Tax Comm'n*, 344 Mass. 503, 509 (1962)(citing *State Tax Comm'n v. John H. Breck, Inc.*, 336 Mass. 277, 299 (1957)). The evidence presented by the appellant in the present appeal lacked credibility and fell far short of that required to sustain its burden.

Thus, on the basis of all of the evidence presented and the reasonable inferences drawn therefrom, the Board found and ruled that the appellant was not entitled to an abatement of sales taxes or § 35A penalties and issued a decision for the appellee in this appeal.

THE APPELLATE TAX BOARD

By: _____
Thomas W. Hammond, Jr., Chairman

A true copy,

Attest: _____
Clerk of the Board