

# State of Alabama Department of Revenue

**VERNON BARNETT**  
Commissioner



**Sales & Use Tax Division  
Mobile Taxpayer Service Center**

## **Confidential Audit Report**



This report contains confidential information that is subject to the provisions of Section 40-2A-10, Code of Alabama 1975.

Examination Conducted by: **Thomas Hogg, Vicky Brunelle**  
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District Supervisor: **Bernice Braswell**  
Date: **October 17, 2017**



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# State of Alabama Department of Revenue

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Deputy Commissioner

October 17, 2017



RE:	TAX TYPE	PERIOD	ACCOUNT #
	Sales Tax	08/01/2014 - 05/31/2017	SLS-R008985833

This report is the result of an examination of the records of [REDACTED] to determine compliance with Sales Tax. This report contains information concerning the company's business activities, records examined, and audit conclusions. The report and attached working papers serve as notification and explanation of the basis for any assessment and penalties in accordance with Section 40-2A-4(a)(3)a., Code of Alabama 1975, as amended.

## Type of Business

[REDACTED] (The Store) has retail operations at [REDACTED]  
[REDACTED] (The Taxpayer) of [REDACTED] is the sole member of this domestic company which was organized in 2014. In July of that year [REDACTED] purchased the above mentioned convenience store. He sells products typically found at convenience stores such as gasoline, groceries, soft drinks, fountain drinks, beer, wine, tobacco, etc.

This location, inside the city limits of Bay Minette subjects retail sales to the following local sales taxes:

Baldwin County  
City of Bay Minette

Non State Administered  
Non State Administered

### **Power of Attorney**

A Power of Attorney, Form 2848A, was signed by [REDACTED] on 6/26/2017 appointing [REDACTED], CPA as his authorized representative.

### **Sales Tax**

#### **Records**

The following records were requested:

1. All books and records used in the preparation of your returns
2. Sales invoices and Sales Journal
3. Z-Tapes and Cash Register Recaps
4. Customer Tax Exempt File
5. Purchase Invoices
6. Depreciation Schedules/Asset Files
7. Federal/State Income Tax Returns
8. Form 1099K, Statement of Payment Card and Third Party Network Transactions
9. Cancelled Checks with Bank Statements
10. Any other records that may be needed during the audit

The Taxpayer provided some purchase invoices and credit card receipts. They were not in good condition or order. The Store had recently installed a point of sale system in place that could generate sales information in detail, but those were after the audit period. Z-tapes from the previous system were not provided or kept.

#### **Method of Reporting**

Timely sales tax returns were filed with The Alabama Department of Revenue (The Department) by [REDACTED]. He told auditors that he used bank statements with cancelled checks to total his wholesale purchases. He multiplied the purchases by his markup factor to compute the amount of taxable sales. Sales were rung up and recorded on a computerized Point of Sale System (POS), but those records were not kept by The Taxpayer.

#### **Audit Procedure**

All retail businesses subject to Alabama sales tax are statutorily required to keep complete and 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. The Taxpayer in this case did not

retain any sales records, reports or register tapes thus failing to provide information to The Department that might have been used to verify his reported sales.

In such cases, The Department is authorized to compute a taxpayer's 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. For these reasons examiners performed an additional taxable audit using the IRS purchase markup method.

Ten vendors from whom wholesale purchases of inventory had been made were identified. Gasoline purchases were not included because sales of Gasoline are not subject to sales tax in Alabama. Purchase records were obtained from those vendors and summarized in columns B through K of Informational Schedule B Comparison of Purchases to Sales Reported.

Tobacco companies give buy-downs (rebates) to retailers once they reach a certain level of purchases. Those rebates effectively reduce amounts retailers pay for inventory. The taxpayer furnished auditors with records of the rebates he received. Credit for them was given in column L of the schedule.

Sales of motor oil and some other automotive products are not subject to sales tax. Credit for those purchases was given in column M of the schedule.

Total purchases of inventory that is subject to sales tax when sold to consumers was totaled in column N of the schedule and is shown below. Taxable sales reported to The Department by The Taxpayer appears in column O. The difference between them is computed in column P.

Comparison of Purchases to Sales Reported			
A	N	O	P
Month Ending	Total Purchases	Sales Reported on Sales Tax Returns	Difference
8/31/2014	37,154.13	36,914.57	-239.56
9/30/2014	49,819.51	44,797.30	-5,022.21
10/31/2014	59,879.62	43,838.52	-16,041.10
11/30/2014	37,134.41	37,479.98	345.57
12/31/2014	50,829.78	39,280.17	-11,549.61
1/31/2015	39,591.18	35,634.84	-3,956.34
2/28/2015	34,240.23	29,678.61	-4,561.62
3/31/2015	37,674.68	36,403.10	-1,271.58
4/30/2015	48,266.34	38,486.30	-9,780.04
5/31/2015	42,976.61	43,087.10	110.49
6/30/2015	48,665.02	44,434.98	-4,230.04
7/31/2015	58,334.39	48,166.65	-10,167.74
8/31/2015	44,495.87	47,494.20	2,998.33
9/30/2015	55,807.46	44,176.08	-11,631.38
10/31/2015	48,136.55	47,556.21	-580.34
11/30/2015	44,788.62	45,839.80	1,051.18
12/31/2015	57,224.40	46,331.33	-10,893.07
1/31/2016	42,125.64	42,659.75	534.11
2/29/2016	44,150.16	39,022.38	-5,127.78
3/31/2016	53,452.87	45,167.00	-8,285.87
4/30/2016	50,001.93	44,978.00	-5,023.93
5/31/2016	53,548.78	46,677.00	-6,871.78
6/30/2016	59,561.63	47,049.00	-12,512.63
7/31/2016	42,282.41	48,456.00	6,173.59
8/31/2016	55,843.87	47,831.27	-8,012.60
9/30/2016	47,822.40	45,977.00	-1,845.40
10/31/2016	47,166.76	48,259.00	1,092.24
11/30/2016	58,661.73	46,388.97	-12,272.76
12/31/2016	46,618.02	43,765.00	-2,853.02
1/31/2017	41,258.92	40,288.00	-970.92
2/28/2017	42,196.84	40,588.00	-1,608.84
3/31/2017	61,489.95	49,660.00	-11,829.95
4/30/2017	48,487.73	50,278.00	1,790.27
5/31/2017	65,335.80	52,121.00	-13,214.80
	1,655,024.24	1,488,765.11	-166,259.13

The above illustration shows that The Taxpayer spent \$166,259.13 more purchasing inventory than he reported in sales.

The purchase amounts shown in column N above were entered on Schedule A Sales. The standard IRS markup percentage currently used by The Department and applicable to convenience stores is 35.54%. It was applied by multiplying monthly purchases by 1.3545 to arrive at the calculated sales that should have been reported. Credit was given in Schedule A for the sales tax measure reported to The Department by the taxpayer subtracting them. The additional taxable amount is the last numeric column in the schedule.

Auditors did not perform local sales tax audits because The Store does not make sales in any

state administered locality.

### Waiver and Statute

A waiver is not needed because a preliminary assessment may be entered **at any time if no return is filed** as required, or if a false **or fraudulent return is filed** with the intent to evade tax. (Section 40-2A- 7(b)(2)(a)). The Department is recommending a 50% fraud penalty. See Basis for Penalties section. However, a waiver was obtained and is valid through January 5, 2018.

### Basis for Assessment

Retail sales of tangible personal property were made to customers in Alabama that were neither taxed or reported in violation of Section 40-2A-4(a)(3)a., Code of Alabama 1975, as amended.

### Basis for Penalties

A 50% fraud penalty was assessed in accordance with Section 40-2A-11(c). The fraud penalty is appropriate for the following reasons

1. [REDACTED] filed monthly sales tax returns himself but did not use sales records as the basis for those returns.
2. [REDACTED] told auditors that he used bank statements with cancelled checks to total his wholesale purchases and then multiplied the purchases by his markup factor to compute the amount of taxable sales. The illustration in the Audit Procedure section above clearly shows that wholesale purchases exceed reported sales by \$166,259.13 or on average by \$4,888 per month.
3. Sales were significantly and consistently under reported. Where acts are part of a consistent pattern, it may be concluded that they are based on an underlying willful intent
4. No reasonable person would conclude that this willful under reporting was done for any other reason than to evade taxes that were legally due.

### Audit Schedules

Schedule A Sales	Additional Taxable Sales
Informational Schedule B	Comparison of Purchases to Sales Reported

### Laws and Rules

The following Sections of Law and Rules were given to the taxpayer as backup for any adjustments made in this examination:

40-23-61	Code of Alabama 1975, Property taxed; persons liable
810-6-4-.06	Failure of Seller to Collect Tax

810-6-4-.10	Keeping Records of Sales For Resale (Formerly Regulation L)
810-6-1-.144.03	Resale, Sales for
810-6-4-.20	Seller Must Pay and Collect Tax Due
810-6-1-.184	Seller Sells Tax Free at the Seller's Risk
810-6-5-.19	Seller to Give Receipt For Tax Collected
810-6-2-.90.01	Seller's Responsibility to Collect and Pay State Sales Tax and Seller's Use Tax
810-6-5-.04.02	Seller's Responsibility to Collect County and Municipal Sales and Use Taxes
810-6-1-.178	Transportation Charges
810-6-1-.179	Transportation Costs, Sellers
810-6-2-.107	Wholesale Sales
810-6-1-.196	Withdrawals From Inventory
810-6-1-.69	Containers, Components of Containers, Labels, Pallets, and Shipping Supplies

### **Contentions**

None were expressed.

### **Response to Contentions**

Not applicable.

### **Recommendations for Improvement**

Records should be maintained including daily sales summary and monthly sales summary generated from the point of sale system. Vendor invoices should be maintained also. The actual taxable sales should be reported and taxes remitted in a timely manner. Baldwin County and The City of Bay Minette should be contacted regarding local sales taxes that may be owed.

### **Liability Summary**

The following is a summary of the audit liabilities. If you are in agreement with the audit liabilities as stated, please remit the total amount due by **September 7, 2017** to avoid additional interest charges. Checks should be made to the order of the Alabama Department of Revenue. Interest will continue to accrue daily on the liabilities until paid in full.

If the liabilities remain unpaid, the file will be forwarded to the central office in Montgomery for assessment/collection proceedings to begin. Please bear in mind that an assessment may require the filing of a tax lien in accordance with the Department of Revenue's policy. The appeal rights are explained in the Taxpayer Bill of Rights pamphlet that was delivered when the examination began and will also be explained in the assessment documents that will be sent from the central office in Montgomery.

Taxes Audited	Tax Due	Interest*	Penalty**	Total
Sales Tax	\$30,118.61	\$1,748.69	\$15,059.37	\$46,926.67
Total	\$30,118.61	\$1,748.69	\$15,059.37	\$46,926.67

\*Interest is calculated to 09/07/17

\*\*Penalty: 50% fraud penalty was assessed in accordance with Section 40-2A-11(c)

A payment in the amount of \$7,000 was made on 9/7/2017, check #3024 with voucher #5645321605R.

### Privilege License

The Taxpayer is properly licensed under sections 069, 072, 106, 144, 153, and 315.

### Closing Remarks

cooperated fully with examiners. He responded promptly when contacted. retained a local CPA to file monthly sales tax returns.

Please note that the information listed in the audit schedules may be forwarded to any applicable county or city that has entered into an exchange of information agreement with the Alabama Department of Revenue.

This report was prepared by:  
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