

THE CENTRAL STOP, LLC
7081 HOWELLS FERRY ROAD
MOBILE, AL 36618-3127,

Taxpayer,

v.

STATE OF ALABAMA
DEPARTMENT OF REVENUE.

§

§

§

§

§

STATE OF ALABAMA
ALABAMA TAX TRIBUNAL

DOCKET NO. MISC. 15-564

FINAL ORDER

The Revenue Department assessed The Central Stop, LLC (“Taxpayer”) for State and Mobile County tobacco tax for February 2012 through June 2013. The Taxpayer appealed to the Tax Tribunal pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on June 3, 2015. John Crowley represented the Taxpayer. Assistant Counsel Duncan Crow represented the Department.

The Taxpayer operated a retail business in Mobile, Alabama during the period in issue at which it sold cigarettes, cigars, and other tobacco products, in addition to gasoline, groceries, beer, etc. The Taxpayer was not authorized under Alabama law to buy or sell untaxed tobacco products during the subject period.

A Revenue Department examiner discovered during the audit of another Alabama tobacco retailer that the Taxpayer had purchased untaxed tobacco products at wholesale from Payless Cash & Carry (“Payless”) in Pensacola, Florida. Because the Taxpayer was not licensed to purchase untaxed tobacco products, the examiner audited the Taxpayer to determine if the Taxpayer was complying with Alabama’s tobacco tax laws.

The examiner requested the Taxpayer’s records from Danh Pham, one of the Taxpayer’s two owners. Pham explained that his business was raided by federal agents in March 2013, and that those agents took most of his records. Pham did provide some

scattered records, which the examiner determined to be insufficient.

Pham told the examiner that he primarily purchased his tobacco products from Wigley & Culp in Mobile. He also purchased some items as needed from the Sam's Club in Mobile. The appropriate tobacco tax had been paid on those products. The examiner asked Pham on several occasions if he had ever purchased untaxed tobacco products from Payless in Pensacola. Pham repeatedly denied that he had ever done so.

The examiner subsequently requested records from Payless. Payless provided a copy of an application to purchase tobacco products in the Taxpayer's name. The application showed Pham as the owner, and the Taxpayer's address as 7081 Howells Ferry Road, Mobile, Alabama, 36618, which is the Taxpayer's business location. The examiner also showed the manager at Payless a copy of Pham's Alabama driver's license and asked if the manager recognized Pham as a customer. The manager stated that he did.

Payless also provided the examiner with a summary of the tobacco products purchased by the Taxpayer from Payless in 2012 and 2013.¹ All of the products had been purchased with cash. The examiner used the purchase information to compute the Alabama tobacco tax owed by the Taxpayer on the products purchased from Payless. The Department accordingly assessed the Taxpayer for the State and Mobile county tobacco tax due. It also assessed the Taxpayer for the 50 percent fraud penalty levied at Code of Ala. 1975, §40-2A-11(h).

¹ The examiner testified that during the period January through June 2013, the Taxpayer purchased 1,290 boxes of cigars and papers from Payless, and only 127 boxes from Wigley & Culp, its primary Alabama supplier.

The Taxpayer argues that there is “no evidence whatsoever that the (tobacco products purchased from Payless) were distributed to any person within the State of Alabama. . . , no inference can be made that the (tobacco products), allegedly purchased in Florida, were actually sold at the Taxpayer’s store.” Taxpayer’s Post-Hearing Brief at 3.

All taxpayer’s are required to maintain accurate and complete records sufficient to allow the Revenue Department to determine the taxpayer’s correct liability. Code of Ala. 1975, §40-2A-7(a)(1). In the absence of such records, or the taxpayer’s failure to file returns, as in this case, the Department is authorized to compute the taxpayer’s liability using the best information reasonably obtainable. Code of Ala. 1975, §40-2A-7(b)(1).

The Taxpayer in this case failed to provide complete records from which its correct tobacco tax liability could be determined. The Taxpayer claims that the federal government took its records in a raid involving illegal “spice” in 2013. It argues that the Department examiner should have requested the records from the federal government. “There was no proof offered that the records did not exist, only that (the Department examiner) did not follow up with federal authorities to seek access to those records.” Taxpayer’s Post-Hearing Brief at 4.

To begin, the statutory duty was on the Taxpayer to maintain good records and to make those records “available for inspection by the department upon request at a reasonable time and location.” Section 40-2A-7(a)(1). Consequently, if in fact the federal government did take the Taxpayer’s records, it was incumbent on the Taxpayer, not the Department examiner, to obtain the records from the federal agency that took the records and make them available for inspection by the examiner. And even if the Taxpayer had provided its records to the examiner, it is doubtful that the records would have shown that

the Taxpayer had purchased untaxed tobacco products from Payless, given the owner's repeated claim that he never purchased tobacco products from Payless.

In any case, the final assessment in issue is based on records provided by Payless showing that the Taxpayer, by and through its owner Danh Pham, had registered to purchase untaxed tobacco products from Payless. A manager at Payless also recognized Pham's picture on his driver's license. Importantly, the Payless records show that the Taxpayer routinely purchased significant volumes of untaxed tobacco products from Payless using cash during the period in issue. Those reliable records constitute the best information available that the Department examiner correctly used in computing the tax due.

The Taxpayer argues that there is no proof that it sold the tobacco products purchased from Payless at its store in Mobile, or for that matter, anywhere in Alabama. Such proof is, however, not required.

The examiner's method of computing the additional tobacco tax owed by the Taxpayer was similar to a purchase, mark-up audit that the Department routinely uses to compute a taxpayer's sales tax liability. The Department performs a purchase mark-up sales tax audit when a taxpayer fails to keep complete sales records, as in this case. In a mark-up audit, the Department examiner obtains the taxpayer's purchase records from the taxpayer's vendors. A reasonable mark-up percent is applied to the taxpayer's total wholesale purchases to determine or estimate the taxpayer's total retail sales. Importantly, it is assumed in a purchase mark-up audit that the retailer/taxpayer sold the merchandise purchased at wholesale in the course of its retail business. The taxpayer may reduce the estimated tax due by showing that some of the merchandise was stolen or destroyed, or is

still in inventory. It is incumbent on the taxpayer, however, to present evidence proving that the merchandise was not sold in the regular course of business.

In this case, the examiner used the records from Payless, one of the Taxpayer's vendors, to compute the additional tax due. And as in a purchase mark-up audit, the Department is not required to prove that the goods purchased from Payless were in fact sold by the Taxpayer at its store in Mobile. Rather, the presumption is that the Taxpayer sold the products at its store. Were it otherwise, a retailer could fail or refuse to keep sales records, and the Department would be required to prove that the retailer sold at retail all of the merchandise previously purchased at wholesale, which would as a practical matter be impossible to do. The presumption that the Taxpayer sold the Payless products at its store in Mobile is reinforced by the fact that (1) the Taxpayer has no other stores in Alabama or elsewhere, and (2) the Taxpayer failed to otherwise explain where the products were otherwise sold, used, consumed, etc.

A final assessment entered by the Department is prima facie correct, and the burden is on the taxpayer to prove that the final assessment is incorrect. Code of Ala. 1975, §40-2A-7(b)(5)c. The Taxpayer has presented no such evidence in this case.

There is also sufficient evidence to affirm the fraud penalty.

Code of Ala. 1975, §40-2A-11(d) levies a 50 percent penalty for any underpayment due to fraud. 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 Department is required to prove fraud by clear and convincing evidence. *Bradford v. C.I.R.*, 796 F.2d 303 (1986). “The burden is upon the commissioner to prove affirmatively by clear and convincing evidence actual and intentional wrongdoing on the part of the (taxpayer) with a specific intent to evade the tax.” *Lee v. U.S.*, 466 F.2d 11, 14 (1972), citing *Eagle v. Commissioner of Internal Revenue*, 242 F.2d 635, 637 (5th Cir. 1957). The existence of fraud must be determined on a case-by-case basis, and 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), citing *Traficant v. Commissioner*, 884 F.2d 258, 263 (6th Cir. 1989). Consequently, fraud may be established from “any conduct, the likely effect of which would be to mislead or conceal.” *Walton*, 909 F.2d at 926, quoting *Spies v. United States*, 63 S. Ct. 364, 368 (1943). The failure to keep adequate records and the consistent underreporting of tax is strong evidence of fraud. *Wade v. C.I.R.*, 185 F.3d 876 (1999) (“There is no dispute (taxpayer) kept inadequate books and records, further suggesting fraud.”).

The Taxpayer argues that the fraud penalty should not be assessed in this case because (1) there is no evidence that it sold the Payless tobacco products in Alabama, and (2) the Department failed to obtain the Taxpayer’s records from the federal agency that confiscated them in 2013.

As discussed, there is no direct evidence that the Taxpayer sold the tobacco products purchased from Payless at its store in Alabama, but as indicated, fraud can be established by cumulative circumstantial evidence.

The evidence is irrefutable that the Taxpayer, by and through its owner Danh Pham, regularly purchased significant amounts of untaxed tobacco products from Payless in Florida during the period in issue. Pham nonetheless has repeatedly denied that he ever purchased tobacco from Payless. That false denial is clear and convincing evidence by itself that the Taxpayer, through Pham, intentionally and knowingly failed to report and pay the applicable Alabama tobacco tax on the Payless tobacco products. The fact that Pham paid for all of the Payless products in cash also shows that Pham was attempting to hide his purchases from Payless.

The final assessment is affirmed. Judgment is entered against the Taxpayer for State and Mobile County tax, penalties, and interest of \$21,121.09 and \$52,702.84, respectively. Additional interest is also due from the date the final assessments were entered, February 17, 2015.

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

Entered August 4, 2015.

BILL THOMPSON
Chief Tax Tribunal Judge

bt:dr

cc: Duncan R. Crow, Esq.
John J. Crowley, Jr., Esq.