

**REDACTED DECISION -- 06-440 W, 06-441 U, 06-442 N, 06-443 C, 06-444 FN -- BY
ROBERT W. KIEFER, JR., ALJ -- SUBMITTED for DECISION on OCTOBER 18, 2007 -
- ISSUED on AUGUST 26, 2008**

SYNOPSIS

1. CONSUMERS' SALES AND SERVICE TAX -- BURDEN OF PROOF -- In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is on the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code § 11-10A-10(e) [2002]; W. Va. Code. St. R. §§ 121-1-63.1 and 69.2 (Apr. 20, 2003).

2. CONSUMERS' SALES AND SERVICE TAX -- BURDEN OF PROOF -- Where an assessment is based on a methodology developed to estimate the amount of tax due, to satisfy its burden of proving that against the assessment is erroneous a taxpayer may not merely demonstrate that the estimated assessment is incorrect, but must provide credible evidence to show the actual amount of tax due.

3. CONSUMERS' SALES AND SERVICE TAX -- BURDEN OF PROOF -- ILLEGAL AND FRAUDULENT CONDUCT -- Intentional illegal or fraudulent conduct by a taxpayer or its principals, agents or employees with respect to a transaction pertaining to one tax may impugn the honesty and credibility of the taxpayer or its principals, agents or employees with respect to other transactions or other taxes.

4. CONSUMERS' SALES AND SERVICE TAX -- BURDEN OF PROOF -- INSUFFICIENT EVIDENCE -- The Petitioner failed to satisfy its burden of proof by reason of its failure to provide evidence to show the actual amount of its sales subject to the consumers' sales and service tax.

5. BUSINESS FRANCHISE TAX -- BURDEN OF PROOF -- In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is on the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code § 11-10A-10(e) [2002]; W. Va. Code. St. R. §§ 121-1-63.1 and 69.2 (Apr. 20, 2003).

6. BUSINESS FRANCHISE TAX -- BURDEN OF PROOF -- Where a business franchise tax assessment is derivative of a consumers' sales and service tax assessment against the taxpayer, the failure of the taxpayer to satisfy its burden of proof with respect to the consumers' sales and service tax constitutes a failure of its burden of proof with respect to the business franchise tax.

7. CORPORATION NET INCOME TAX -- BURDEN OF PROOF -- In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is on the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code § 11-10A-10(e) [2002]; W. Va. Code. St. R. §§ 121-1-63.1 and 69.2 (Apr. 20, 2003).

8. CORPORATION NET INCOME TAX -- BURDEN OF PROOF -- Where a corporation net income tax assessment is derivative of a consumers' sales and service tax assessment against the taxpayer, the failure of the taxpayer to satisfy its burden of proof with respect to the consumers' sales and service tax constitutes a failure of its burden of proof with respect to the corporation net income tax.

9. PURCHASERS' USE TAX -- BURDEN OF PROOF -- In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is on the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code § 11-10A-10(e) [2002]; W. Va. Code. St. R. §§ 121-1-63.1 and 69.2 (Apr. 20, 2003).

10. PURCHASERS' USE TAX -- PAYMENT OF CONSUMERS' SALES AND SERVICE TAX -- Presentation of an invoice showing that a taxpayer paid consumers' sales and service tax with respect to an individual purchase will relieve said taxpayer of a purchasers' use tax assessment with respect to said purchase.

11. PURCHASERS' USE TAX -- COMMON AREA MAINTENANCE PROVISION IN LEASE -- A common area maintenance provision in a lease involves a charge for the provision of services, as opposed to rent for the leasehold interest and, as such, is subject to purchasers' use tax absent some evidence that the services provided are otherwise exempt.

12. PURCHASERS' USE TAX -- PURCHASES USED AND CONSUMED IN BUSINESS -- Items purchased by a taxpayer and used or consumed in its business are subject to the purchasers' use tax.

13. PERSONAL INCOME WITHHOLDING TAX -- BURDEN OF PROOF -- In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is on the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code § 11-10A-10(e) [2002]; W. Va. Code. St. R. §§ 121-1-63.1 and 69.2 (Apr. 20, 2003).

14. PERSONAL INCOME WITHHOLDING TAX -- BURDEN OF PROOF -- ILLEGAL AND FRAUDULENT CONDUCT -- The intentional illegal or fraudulent activity by a taxpayer or its principals, agents or employees, such as filing a W-2 showing that one employee received another employee's income, may impugn the validity of all transactions engaged in by that taxpayer.

15. PERSONAL INCOME WITHHOLDING TAX -- BURDEN OF PROOF -- Where an assessment is based on a methodology developed to estimate the amount of tax due, to satisfy its burden of proving that against the assessment is erroneous a taxpayer may not merely demonstrate that the estimated assessment is incorrect, but must provide credible evidence to show the actual amount of tax due.

16. PERSONAL INCOME WITHHOLDING TAX -- BURDEN OF PROOF -- INSUFFICIENT EVIDENCE -- The Petitioner failed to satisfy its burden of proof by reason of its failure to provided sufficient evidence to show the actual wages paid to its employees and the amount of personal income tax withheld from such wages and paid to the State of West Virginia.

FINAL DECISION

A tax examiner with the Field Auditing Division (“the Division”) of the West Virginia State Tax Commissioner’s Office (“the Commissioner” or “the Respondent”) conducted an audit of the books and records of the Petitioner. Thereafter, on July 13, 2006, the Director of this “Division” issued a consumer’s sales and service tax assessment against the Petitioner. The assessment was issued pursuant to the authorization of the State Tax Commissioner, under the provisions of Chapter 11, Articles 10 and 15 of the West Virginia Code. The assessment was for the period of January 1, 2003, through January 31, 2006, for tax in the amount of \$_____, interest in the amount of \$_____, computed through August 31, 2006, and additions to tax in the amount of \$_____, for a total assessed tax liability of \$_____. Written notice of this assessment was served on the Petitioner.

Also, on July 13, 2006, the Commissioner (by the “Division”) issued a business franchise tax assessment against the Petitioner, under the provisions of Chapter 11, Articles 10 and 23 of the West Virginia Code, for the period of January 1, 2003, through December 31, 2005, for tax in the amount of \$_____, interest in the amount of \$_____, computed through August 31, 2006,

and additions to tax in the amount of \$_____, for a total assessed tax liability of \$_____.
Written notice of this assessment was served on the Petitioner.

Also, on July 13, 2006, the Commissioner (by the “Division”) issued a corporation net income tax assessment against the Petitioner, under the provisions of Chapter 11, Articles 10 and 24 of the West Virginia Code, for the period of January 1, 2003, through December 31, 2005, for tax in the amount of \$_____, interest in the amount of \$_____, computed through August 31, 2006, and additions to tax in the amount of \$_____, for a total assessed tax liability of \$_____.
Written notice of this assessment was served on the Petitioner.

Also, on July 13, 2006, the Commissioner (by the “Division”) issued a purchasers’ use tax assessment against the Petitioner, under the provisions of Chapter 11, Articles 10 and 15A of the West Virginia Code, for the period of October 1, 2001, through March 31, 2006, for tax in the amount of \$_____, and interest in the amount of \$_____, computed through August 31, 2006, for a total assessed tax liability of \$_____. Written notice of this assessment was served on the Petitioner.

Also, on July 13, 2006, the Commissioner (by the “Division”) issued a personal income withholding tax assessment against the Petitioner, under the provisions of Chapter 11, Articles 10 and 21 of the West Virginia Code, for the period of January 1, 2003, through December 31, 2005, for tax in the amount of \$_____, interest in the amount of \$_____, computed through August 31, 2006, and additions to tax in the amount of \$_____, for a total assessed tax liability of \$_____. Written notice of this assessment was served on the Petitioner.

Thereafter, by mail postmarked August 8, 2006, received on August 10, 2006, the Petitioner timely filed with this tribunal, the West Virginia Office of Tax Appeals, a separate

petition for reassessment of each assessment. W. Va. Code §§ 11-10A-8(2) [2007] & 11-10A-9(a)-(b) [2005].

Subsequently, notice of a hearing on the petition was sent to the Petitioner and a hearing was held in accordance with the provisions of W. Va. Code § 11-10A-10 [2002].

FINDINGS OF FACT

1. Ms. A is a Tax Examiner for the State Tax Commissioner and has been so employed for 16 years.

2. In that capacity, she conducts audits of businesses, both in state and out of state for the State Tax Commissioner.

3. Ms. A, along with another Tax Examiner, Ms. B, audited the Petitioner who operates a Mexican restaurant located in West Virginia. As a result of their audit, the five above-referenced tax assessments were issued pursuant to the authority of the State Tax Commissioner. *See State's Exhibit Nos. 1, 3, 4, 5 and 7.*

4. Mr. C, the President of the Petitioner, testified that through several businesses he operates several restaurants, including restaurants in 2 cities in WV and in New York.

5. Mr. C resides in a city in West Virginia.

6. Mss. A and B first visited the Petitioner's place of business on or about March 31, 2006.

7. They contacted the manager, who Ms. A identified as Mr. D, and made some business-related inquiries and took a tour of the restaurant.

8. At that time, Ms. A indicated that she and Ms. B wanted to return on April 3, and requested that the Petitioner make available all of its business records at that time.

9. Mr. D gave Mss. A and B directions to the office of the Petitioner's certified public accountant, to see if he had any of the necessary records.

CONSUMERS' SALES AND SERVICE TAX

10. In touring the restaurant on March 31, 2006, Mss. A and B observed that the Petitioner had a single cash register and an adding machine next to the cash register. It appeared to them that some sales were being rung up on the cash register and some were not.

11. Customers were given guest checks, which were used to ring up sales.

12. They asked Mr. D if he kept cash register tapes, "Z" tapes or other records of sales. When advised that he did not keep such records, Ms. A advised him that he needed to do so and to start ringing up sales.

13. A "Z" tape is tape that is normally run at the end of the day showing a summary of the day's sales, sometimes broken down by category. It will show consumers' sales and service tax collected, and if there were any "Void Sales" or "No Sales," and the amount of any "Void Sales."

14. On March 31, Mr. D clearly told Mss. A and B that no cash register tapes existed, because the register was broken.

15. On March 31, 2006, Mr. D told them that someone broke into the restaurant in January, 2006, stole their safe and damaged the cash register. According to Mr. D, this was the reason the cash register was not working properly.

16. Mr. D advised them that the safe and the cash therein had been recovered.

17. They determined the cash in the safe amounted to \$_____. See State's Exhibit No.

2. Ms. A stated that she would not expect a restaurant to keep that much cash in its safe, as

opposed to depositing it in a bank. She would normally expect a restaurant to keep only cash sufficient to maintain the cash drawer and make change for some larger bills.

18. Mr. C testified that approximately \$5,000 in the safe was due to the large number of gift certificates they sell during the holiday season, November through January.

19. He testified that most people pay cash for the gift certificates. The cash is placed in the safe until the gift certificates are redeemed. When gift certificates are redeemed, that amount of cash is removed from the safe and deposited in the bank.

20. Mr. C testified that the Petitioner will sometimes retain a week's worth of receipts in the safe before depositing them in the bank.

21. Mr. C testified that some of the funds in the safe were his personal funds.

22. He testified that around that time he sold a truck. Although he does not recall how much he derived from the sale of the truck, the proceeds were kept in the safe.

23. He also recalls that money collected from a Pepsi machine was kept in the safe.

24. Mss. A and B returned to the Petitioner's place of business on the following Monday, April 3, 2006.

25. Some records were provided at that time. These included some sales summary sheets, some purchases, and a few consumers' sales and service tax and unemployment compensation tax returns.

26. Mss. A and B began auditing the records at that time.

27. Upon leaving, Ms. A left a handwritten list of additional records that they wanted to review. This included Federal Tax returns, employee W-2s, some months' sales summaries, cash register tapes and "Z" tapes, general ledgers and other records that had not yet been provided.

28. On June 1, 2006, the auditors returned to the restaurant. The Petitioner may have provided some additional records, but few of the requested records were available.

29. Mss. A and B arrived prior to opening and stayed until the restaurant closed that evening.

30. Mss. A and B decided to observe the Petitioner's customers as they entered and left the premises. They kept a listing of the number of people being served and other information respecting those customers. *See* Schedule D, State's Exhibit No. 1.

31. It appeared that there was one guest check per table, even when there was more than one customer and their orders were rung up separately.

32. They observed that some sales were rung up on the cash register, but some were not.

33. Ms. A testified that it appeared that all credit card/debit card sales were rung up on the cash register, but that at least some cash sales were rung up only on the adding machine. She testified that it was somewhat difficult to see from where they were seated, so she could not be certain. It was also difficult to be certain when an entire table would go up to the cash register at the same time, and some customers appeared to pay with a credit card, while others appeared to pay cash.

34. On June 1, they observed that the Petitioner had a newer or different cash register.

35. They could see that the cash register was being used because the lights would illuminate. They did not see the cash register produce any tape. Mr. D told them that there was no cash register tape.

36. Mr. C testified that the cash register at location A does not create a tape. The cash register could create a tape, but he does not know how to put a tape in the register.

37. The cash register does not report the total number of sales for a given day.

38. There is no electronic or other machine record of the number of sales or the amount of sales for any given day.

39. Mr. C testified that he never had tape in his cash register from the day that location A opened.

40. The first machine could accept a tape to record daily sales, but he did not think a tape was necessary because he trusted his manager, Mr. D.

41. The CPA testified that sometimes the Petitioner used tape in the cash register and sometimes it did not.

42. Mss. A and B observed that there were eighty-three (83) tables seated on June 1, 2006, and that there should have been an equal number of guest checks at the end of the day. They asked for all of the guest checks and received eighty (80). Ms. A felt comfortable that they received all guest checks.

43. Ms. A testified that she did most of the work preparing the numbers, including recording information from the guest checks and credit card/debit card tickets.

44. For each guest check, Mss. A and B recorded the amount of the sale, the consumers' sales and service tax charged, the total of the check and any other information on the check. *See* Schedule D-1, Petitioner's Exhibit No. 1.

45. On June 1, 2006, Mss. A and B again requested the cash register tape at the end of the day, but were advised by Mr. D that there was no cash register tape or "Z" tape.

46. They also reviewed credit card receipts for customers who paid with a credit card. Credit card receipts were attached to the guest checks.

47. The credit card/debit card ratio was based on the total, as shown on Schedule D-1, State's Exhibit No. 1.

48. They also made a listing of the credit card and debit card customers, showing the sale, the tip and the total paid to the Petitioner. *See* Schedule D-1-a, Petitioner's Exhibit No. 1.

49. Comparing the sales on Schedule D-1-a to those on Schedule D-1, they determined that credit and debit card sales were approximately thirty and sixty-nine one hundredths of a percent (30.69%) of total sales for that day.

50. The gross sales for that day, \$_____, were higher than the gross sales for any single day in any of the twenty-seven monthly sales summaries provided by the Petitioner.

51. The sales summaries provided by or on behalf of the Petitioner are included in the audit work papers prepared by Mss. A and B. *See* Schedule E, State's Exhibit No. 1.

52. The Petitioner provided bank deposit tickets which corresponded with the cash deposit amounts shown on the sales summaries for any given day. *See* Schedule E, State's Exhibit No. 1.

53. For each month's sales summary, Mss. A and B calculated the percentage of sales shown that were credit card/debit card sales, that were check sales and were cash sales. The percentage of credit card sales ranged from approximately 45% to approximately 83%. *See* Schedule E, State's Exhibit No. 1.

54. As reflected on bank statements, the auditors concluded that the credit card sales were being accurately reported.

55. They also concluded that check sales were being accurately reported.

56. Comparing the percentage of credit card sales on the day they conducted their survey and the percentage as shown on the monthly summaries, Mss. A and B concluded that sales, specifically cash sales, were being under reported.

57. On June 7, 2006, they returned to the restaurant from opening until about 3:00 p.m. and conducted the same type of observation. Again, they observed sales not being rung up on the cash register.

58. Based on their calculations, the credit card/debit card sales for June 7, 2006, were approximately 26%.

59. The results of the June 7, 2006 observation were not used by Mss. A and B. Had they used these results, the assessment would have been greater.

60. The assessment is based on an estimate of additional cash sales for the audit period which, based on their observations, had not been reported by the Petitioner.

61. Having determined that cash sales were underreported, Ms. A and Ms. B developed a methodology to calculate the amount by which they were underreported.

62. They first took the amount of the reported sales paid by cash and check and the sales paid by credit and debit card, which include consumers' sales and service tax, and deleted the tax from the total reported sales by dividing by one and six one-hundredths (1.06).

63. Assuming that credit and debit card sales constituted 30.69 percent of total sales, based on their observations of June 1, 2006, they then took the reported credit and debit card sales for each month, divided them by 30.69 percent (.3069) to arrive at the estimated total taxable receipts (sales) for that month.

64. They computed estimated under reported sales by subtracting the reported credit and debit card sales and the reported cash and check sales from the calculated total estimated sales.

65. They then multiplied the estimated under reported sales by six percent (6%) to arrive at the consumers' sales and service tax to be assessed.

66. The Petitioner did not provide sales summaries for January, 2003, to September, 2003, and for March, 2005, so the auditors estimated the sales for those months by using the average of all other months for which they calculated under reported sales.

67. Mss. A and B also considered using the Petitioner's cost of goods sold to compute the amount of their gross sales, but ultimately determined not to use this method since the Petitioner was not reporting all of its costs of goods sold because it paid for a number of its purchases with cash.

68. With respect to purchase invoices, they looked at every invoice provided, reviewing each one line-by-line, picking up items subject to purchasers' use tax.

69. They concluded that there was not enough purchase invoice information available to perform a cost-of-goods-sold analysis.

70. Ms. A testified that the assessment constitutes her and Ms. B's best estimate of the amount of under reported sales for the years of the audit period.

71. Ms. A admitted that the percentage of credit card and debit card sales fluctuated, increasing as time went on.

72. Even if the sales for June 1, 2006 hadn't been higher than most days shown on the sales summaries, and the ratio of credit card/debit card sales had remained at 30.69%, Ms. A testified that they would have still done what they did because there were other factors that made them think that sales were being under reported.

73. Ms. A emphasized that what she and Ms. B really wanted to see were cash register tapes and the "Z" tapes.

74. One of the days they were at the Petitioner's location, Mss. A and B requested guest checks from the previous day but they were not provided.

75. They concluded that the one-day analysis was sufficient, since they went a second day and determined that the percentage of credit card/debit card sales was less.

76. The Petitioner's certified public accountant, testified on behalf of the Petitioner.

77. The CPA testified that at the end of each month, the Petitioner provided him with a monthly sales summary.

78. The Petitioner submitted a report of sales for August, 2007. *See* Petitioner's Exhibit No. 1.

79. The Petitioner's sales for the month of August, including consumers' sales and service tax was \$_____. The taxable sales were \$_____. Every month The CPA gets a document of this nature showing the sales for the month.

80. On September 26, 2007, the CPA went to the Petitioner's business location and performed the same sort of analysis of the Petitioner's sales for that day as Mss. A and B performed for June 1, 2006.

81. The CPA compared the total sales on September 26, 2007, to the average of all sales on Wednesdays in August, 2007, and determined that the amounts were fairly comparable.

82. The CPA also looked at Wednesday sales in September, 2007, and they were comparable.

83. The CPA testified that the percentage of credit card sales can fluctuate substantially from day to day.

84. The CPA has reviewed State's Exhibit No. 1, and is comfortable with the amount of sales reported to him by the Petitioner.

85. The Petitioner's sales were substantially higher than other comparable restaurants in location A.

86. The CPA has no reason to believe that the Petitioner's total sales were under reported. He never looked at the issue until the time of the audit.

87. He would not be comfortable using a credit card/debit card sales to cash sales ratio for a single day, because it fluctuates substantially from day to day.

88. The CPA believes that this percentage would require a study of at least ten (10) days.

89. The CPA testified that he believed the sales might have been substantially higher on June 1, 2006, because that was around the time of high school graduations in a county in WV. Many families go to the Petitioner's restaurant in conjunction with graduation.

90. The CPA testified that he has seen a gradual increase in sales for the Petitioner each year that it has been in operation. He estimates that the increase is approximately 10% per year.

91. In 2006, the Petitioner paid approximately \$_____ in consumers' sales and service tax. In 2007, it was projected to pay approximately \$_____ in consumers' sales and service tax.

92. The CPA is familiar with the methodology of the Petitioner's monthly sales summaries.

93. At the end of the day, the guest checks are totaled. The manager does this, adding up the guest checks by hand on an adding machine.

94. The guest checks may not be destroyed at the end of the evening, but they are not retained for any extended period of time.

95. The monthly sales summary is the only document that is provided by the Petitioner to the CPA.

BUSINESS FRANCHISE TAX

96. The franchise tax assessment is an estimate based on estimated under reported sales for purposes of the consumers' sales and service tax, which are treated as retained earnings.

97. The franchise tax assessment also takes into account the withholding tax assessment, because the additional withholding tax assessed would constitute an expense that would reduce Petitioner's assets, specifically retained earnings, for purpose of the franchise tax.

98. The CPA testified that he believed the Petitioner's sales were reported correctly to both him and to the State Tax Commissioner. Therefore, there would be no increase in the Petitioner's retained earnings and, therefore, no additional business franchise tax.

99. The CPA further testified that if additional withholding was attributable to the Petitioner, then there would be additional wages and salary paid to its employees, which would reduce retained earnings.

100. The CPA also testified that he sees monthly receipts from their supplier of produce, dishwashing liquid and other similar items, and that the Petitioner also purchases items from Wal-Mart, which reduces their retained earnings.

101. The Tax Commissioner concedes that if the Petitioner prevails on the consumers' sales and service tax, then there should be no business franchise tax assessment.

CORPORATION NET INCOME TAX

102. The amount of the corporation net income tax assessment reflects the additional income attributable to the Petitioner as a result of its failure to report all of its sales.

103. The Petitioner is a "C" corporation, so the corporation is subject to corporation net income tax.

104. The CPA testified that his testimony with respect to the business franchise tax also applies to the corporation net income tax.

105. The Tax Commissioner concedes that if the Petitioner prevails on the consumers' sales and service tax, then there should be no business franchise tax assessment.

PURCHASERS' USE TAX

106. A substantial portion of the Petitioner's purchases are for resale to the restaurant's customers.

107. Part of the assessment results from the failure of the Petitioner to have evidence showing that consumers' sales and service tax was paid on items used and consumed in the business, such as paper products, film, cleaning supplies and common area maintenance.

108. The remainder of the assessment results from the failure of the Petitioner to pay consumers' sales and service tax on certain equipment and leasehold improvements.

109. The Petitioner presented an invoice with its memorandum of law to show that consumers' sales and service tax was paid with respect to the leasehold improvements.

110. Ms. A testified that she was unaware of the type of restaurant equipment that was purchased or the vendor from whom the equipment was purchased.

111. With respect to the other two items, the CPA testified that he is unaware of the type of restaurant equipment that was purchased. He also testified that he is not certain that consumers' sales and service tax or purchasers' use tax was paid on either purchase, and he is unable to ascertain whether or not such tax was paid.

112. Ms. A testified that they made an effort to separate out purchases of items that are provided to customers as part of the sale, such as "to go" containers and plastic ware for carry out items.

113. The CPA reviewed both State's Exhibits Nos. 5 & 6.

114. He knows that the leasehold improvement expense was money paid to a contractor for renovating the restaurant from its former condition to accommodate a Mexican restaurant.

115. The CPA testified that the common area maintenance was part of the rent paid to the landlord, which is for the purpose of maintaining common areas of the plaza in which the restaurant is located.

116. The CPAr does not have a copy of the lease and has not seen a copy.

117. The checks are written to the owner of the plaza where the restaurant is located.

118. Ms. A testified that the common area maintenance was broken out as a separate charge, but that the Petitioner wrote a single check to pay for both the premises and the common area maintenance

119. Ms. A testified that the common area maintenance charge commenced in April, 2005. She has never seen the lease

WITHHOLDING TAX

120. While at the Petitioner's location on March 31, 2006, Mss. A and B observed a manager, four waiters serving tables and four men working in the kitchen, a total of nine employees. All were male.

121. When asked about nine employees working a full thirteen hours per day, Ms. A testified that it appeared that all nine employees were present and working the entire day. It did not appear that any employees left during the day.

122. The use of only two employee numbers on guest checks seemed odd to the auditors, but they assumed that multiple employees were using the same numbers.

123. They toured the kitchen on both March 31, 2006, and April 3, 2006,.

124. They requested payroll records, including employee W-2s, returns, payroll summary sheets and any payroll records in the Petitioner's or the CPA's possession.

125. Eventually they received employee W-2s and some unemployment compensation records.

126. The CPA indicated that other payroll records were in the monthly packets returned to the taxpayer. It also provides its payroll every two weeks.

127. Mss. A and B could not find the payroll records for any of the months that they reviewed.

128. On March 31, 2006, Ms. A asked Mr. D for an employee work schedule, and was told that he did not have one.

129. At some point, Mr. D told Ms. A that the employee work schedule was thrown away at the end of the day.

130. When Ms. A asked Mr. D to write down the names of the employees who were working on March 31, he wrote down some names, including several women. Ms. A requested all of the names, but Mr. D never wrote down the names of all of the employees working that day.

131. They concluded that withholding was underreported because: 1) The Petitioner lacked certain payroll records; 2) They considered the total of wages paid to the employees on an annual basis to be relatively small given the number of people they observed working at the restaurant and the number of hours the restaurant was open; 3) There was withholding reported for female employees, but no female employees were observed working at the restaurant; 4) Mr. D's reluctance to identify all of the employees working at the restaurant; and 5) They could find no

record of withholding for the manager, Mr. D, although they knew he had been an employee since 2004.

132. She looked at the W-2s for each year.

133. The total wages for 2003, 2004 and 2005 were in the range of \$_____ to \$_____ for all employees for each of the three years.

134. The W-2s reviewed by the auditors are detailed in the audit work papers. They list the employees' names, Social Security numbers, gross wages and West Virginia withholding.

135. This detail is listed on Schedule A-1, State's Exhibit No. 7 for each of the three years.

136. There was no evidence that wages were paid to Ohio residents.

137. Each day they observed employees at the Petitioner's location, the workers were all male, yet the withholding tax information shows a majority of female employees.

138. Each time they went to the Petitioner's location, they dealt with Mr. D, the manager. Because Mr. D had signed for food purchases since at least April, 2004, they knew he was an employee.

139. No W-2s were issued to Mr. D for any of the audit years.

140. When they returned to the Petitioner's location, they were not sure how many employees were working, because they did not tour the kitchen.

141. Based on their observation respecting the number of waiters and the employees they saw entering and exiting the kitchen, they estimated that there were six to nine employees, including Mr. D.

142. Believing withholding tax had been underpaid, the auditors developed an estimate of the amount that should have been withheld from the Petitioner's employees.

143. Mss. A and B made some calculations based on observations made by them.

144. In estimating the number of hours that employees worked, they began with the number of hours that the restaurant was open and added an hour before opening for preparation and cooking, and an hour after closing for closing and cleaning.

145. The determined that the restaurant was open thirteen (13) hours Monday through Saturday, except thirteen and one-half (13 ½) hours on Friday and eleven and one-half (11 ½) hours on Sunday, for a total of ninety (90) hours worked per week. Multiplying this figure by 52 weeks, they estimated that an employee worked four thousand six hundred and eight hours per year.¹ They assumed six annual holidays of thirteen (13) hours on which employees did not work, and deducted that from the estimated number of hours worked annually. They then divided the estimated annual hours worked by twelve to arrive at estimated monthly hours worked. *See* Schedule A-2-a, State's Exhibit No. 7.

146. Mss. A and B performed a similar calculation for weekends, assuming the Petitioner might have additional employees on weekends, when there was more business. *See* Schedule A-2-a, State's Exhibit No. 7.

147. They took the estimated hours worked by cooks and waiters and multiplied that by \$5.15, the hourly minimum wage. They took the estimated hours worked by a manager and multiplied that by \$10.00, an estimated hourly wage. These figures resulted in estimated monthly wages. *See* Schedule A-2, State's Exhibit No. 7.

148. They took the monthly estimated wages, subtracted the monthly reported wages to arrive at the estimated monthly under reported wages. *See* Schedule A-2, State's Exhibit No. 7.

¹ The methodology does not assume that a particular individual necessarily worked that many hours per year. Instead, the theory is that a particular slot ("Waiter 1" or Cook "3") was filled by one or more employees for that many hours over the course of the year.

149. They then calculated the estimated tax that should have been withheld on the monthly estimated wages for each employee. From the estimated total tax that should have been withheld, they deducted the amount actually withheld, to arrive at the amount of tax assessed. *See Schedule A-2, State's Exhibit No. 7.*

150. Ms. A is not certain that all of the employees arrived one hour before the restaurant opened and is not certain that all of the employees stayed one hour after the restaurant closed.

151. The estimated hourly wage for the manager was just a guess on their part as to what would constitute a fair wage.

152. The hourly wage for the cooks and waiters was minimum wage. However, waiters are not required to be paid minimum wage, because they receive tips.

153. The estimated withholding for "Waiter 3" for December is more than the withholding for the other positions. Ms. A was not sure why this was the case.

154. She did not notice employees working in dual capacities. Waiters were going into and coming out of the kitchen.

155. They also noticed that Mr. C was the highest paid employee although, according to Mr. D, Mr. C did not work at the restaurant on a consistent basis and did not stop by the restaurant that frequently.

156. She saw four people waiting tables, but couldn't say that all four were distributing guest checks.

157. The estimated total wages for 2003 were \$_____. Estimated gross receipts for the restaurant were \$_____. Thus, wages were 34% of gross receipts.

158. She does not know whether this percentage is an average amount. This is not something she would look at on a regular basis.

159. During his observations on September 26, 2007, the CPA observed about five employees. There was a waiter and a waitress, two cooks and a bus boy. The bus boy also helped wait tables.

160. The CPA observed a waitress leave during a slow period, between 1:30 p.m. and 5:30 p.m., and a waiter leave for an unspecified period of time.

161. He is not sure if the kitchen employees stayed there the whole day.

162. He patronizes the restaurant. He has never seen more than one or two waiters and waitresses.

163. The CPA is of the opinion that the restaurant would not survive financially if it had to pay seven employees thirteen hours per day seven days per week.

164. He is not certain if they pay six to seven employees on some days.

165. When the Petitioner reports payroll, it is broken down into the number of hours an employee works for a two-week period.

166. Some of the employees get paid \$2.13 per hour, some get paid \$5.65 per hour and some get paid \$6.00 per hour.

167. The most he has seen anyone work in a two-week period, as shown on a summary, is eighty hours.

168. Generally speaking, payroll as a percentage of gross receipts is approximately ten percent over a broad spectrum of businesses.

169. For restaurants, the norm is about ten to twelve percent, because a lot of what is reported are tips, although withholding is paid on tips.

170. A restaurant operating at above thirty percent (30%), considering the cost of goods sold, would be unable to survive.

171. The CPA reviewed the W-2 summary reviewed by the auditors and has no reason to believe that it is inaccurate, and that it does reflect the actual number of hours worked.

172. The CPA believes that the estimated withholding calculation is impossible.

173. The CPA testified that for 2005, there was nothing withheld for Mr. D.

174. The CPA testified that he recently found out that Mr. D's wages were paid to Mr. C and tax withheld in Mr. C's name. Mr. C then paid the wages over to Mr. D. Mr. D is a relative of Mr. C.

175. So far as the CPA knows, Mr. D does not have a Social Security number, but is in the process of getting one.

176. The CPA does not believe it should be handled in this manner and has so advised Messrs. C and C.

177. The CPA testified that Ms. E is Mr. D's wife and she also may get paid for him.

178. Mr. C testified that he sometimes worked in the kitchen.

179. The CPA does not know whether the wages paid to Mr. C in 2003 were paid to him, or whether they might have been paid to someone else.

180. The Petitioner withholds taxes from the employees on the tip income and remits the same to the government.

181. The CPA believes the withholding is accurate based on wages paid to hours worked.

182. When asked to identify employees named in the W-2s, the CPA identified them either as managers or waiters and waitresses. The CPA did not identify anyone who was a cook for whom there was a W-2.

DISCUSSION

PETITIONER'S ILLEGAL AND FRAUDULENT ACTIVITIES

At the time that Mss. A and B audited the Petitioner, they saw and were told things that caused them to believe that the Petitioner was not properly reporting and paying its taxes. Certain things caused them to believe that the actions of the Petitioner's principals were knowing and intentional, and not just due to negligence or lack of knowledge of the law and its requirements. The evidence presented at the hearing justifies their conclusions.

There is clear evidence in the record of the Petitioner's intent to evade the law. It relates to the payment of Mr. D's wages. The evidence shows that Mr. D was an employee of the Petitioner from at least some time in 2004. Yet no W-2s exist to show that the Petitioner ever paid wages to Mr. D. Nothing exists to show that the Petitioner ever paid any withholding on wages paid to Mr. D. The CPA's testimony, that Mr. D's wages were being paid to Mr. C or under his Social Security number, shows why no such records exist.² This demonstrates the Petitioner's clear intent to violate the law. Mr. C must have been involved since Mr. D's wages were credited to him. The evidence shows clear fraud on the part of the Petitioner and, specifically, Messrs. C and D.

Mr. C's silence in the face of his certified public accountant's testimony of fraud and illegality speaks volumes. If the CPA's testimony were not true, one would expect Mr. C to take issue with it. Instead, he allowed this testimony to go un rebutted. This is clear evidence of fraud, that borders on an admission. Given this testimony, it is not unwarranted for this Office to consider the remainder of the Petitioner's evidence to be suspect. Stated differently, this evidence of fraud taints every aspect of the Petitioner's evidence, except that which is subject to independent, objective verification.

² The CPA clearly recognized that this was problematic and advised the Petitioner to correct this situation. According to the CPA, Mr. D was in the process of obtaining a Social Security number.

There is an apparent lack of congruence between the W-2s produced by the Petitioner and the identity of the employees working in the restaurant. The W-2s show that the Petitioner employed twelve people in 2003, eight of whom were female. It employed eight people in 2004, six of whom were female. It employed seven people in 2005, four of whom were female.³ Yet, on the day the auditors were in the restaurant, they saw nine employees, all male. On the day that the CPA conducted his survey, he saw only a single female employee. Additionally, as pointed out by counsel for the State Tax Commissioner, when the CPA was asked to identify the position of each individual who received a W-2 by name, he identified them all as either waiters or managers. He did not identify any of the employees as cooks. The W-2s and the W-2 summaries do not appear to match the employees working at the restaurant. Given the evidence of fraud, it is not an unwarranted conclusion that this is further evidence of fraud.

Also questionable is the Petitioner's failure to maintain certain personnel records. When the auditors showed up at the restaurant, they asked Mr. D for a list of the employees working that day. Ms. A testified that he listed some employees, but not all. When questioned about that, he listed a couple of more names, but again not all. When asked for a daily work schedule for employees he stated that there wasn't one, which seems unlikely. Another time he told the auditors that he destroyed work schedules at the end of the day, contradicting his statement that there was no schedule. These actions are evidence of evasion on his part. Given Mr. D's participation in other fraud, this also is tainted with fraud.

The evidence respecting the Petitioner's sales is also suspect. The only documentary evidence respecting sales are the monthly summaries prepared by the Petitioner's employees and submitted to the CPA. The Petitioner did not produce an electronic record of daily sales, such as

³ None of the employees listed was Mr. D. Mrs. E and Mr. C were two of the listed employees.

a cash register tape and a “Z” tape, to verify its summaries.⁴ The Petitioner’s employees also rang up sales on an adding machine, not the cash register. This speaks for itself. This evidence tends to call into question the reliability of the monthly sales summaries, rather than bolster it.

The fact that Mr. C and/or the Petitioner kept a substantial amount of money in the safe is also suspect. While not *ipso facto* evidence that the Petitioner is not reporting all of its cash sales, it can be evidence that that is what occurred.

Mr. C’s explanation for why such a large sum of money was kept in the safe is less than convincing. He testified that part of the money was the proceeds of the sale of gift certificates, and then described a rather circuitous method for redeeming gift certificates. His explanation that some of the funds were the proceeds from the sale of his personal truck is plausible. However, it is hard to believe that Mr. C would commingle his and the Petitioner’s funds in this manner. Some documentation verifying the sale would be of value. However, Mr. C offers nothing but his word. In light of his fraudulent conduct, the lack of independent verification renders his unsupported testimony suspect.

The totality of the evidence in the record respecting the Petitioner’s business practices, certainly supports the conclusion that the Petitioner was under reporting its cash sales. It also supports the conclusion that at least some portion of the cash in the safe was from under reported sales. Given the amount of money that the Petitioner was collecting on a day-to-day basis versus the amount of money it was depositing to its bank account, it is a reasonable conclusion that the Petitioner's management was not reporting a portion of its cash sales.

The testimony presented by the Petitioner’s witnesses in this matter is belied by the state of its business records. The Petitioner’s records are either non-existent (employee work

⁴ This clearly raised the suspicion of the auditors.

schedules, cash register tapes and “Z” tapes), fraudulent (Mr. C’s W-2) or a mess (employee W-2s that tend to contradict what was actually happening). Maintenance of detailed, accurate business records should be the norm. Instead, the Petitioner’s business records, to the extent they exist, are sparse and shoddy. In large measure they are inaccurate. In fact, it appears that they may be, at least in part, intentionally inaccurate. Given the evidence of the Petitioner’s fraudulent actions, attribution of the Petitioner’s actions to benign causes or neglect is negated. In fact, the Petitioner’s fraudulent actions taint every aspect of this matter. Accordingly, the Petitioner’s business records and Mr. C’s testimony will be given little to no weight.

The CPA does little to contradict this conclusion. His testimony is based, in large measure on records he was furnished by the Petitioner and on representations made to him by Mr. C and the Petitioner’s employees. The CPA’s sources of information are not reliable. To the extent that Mr. C and the Petitioner intended to deceive the State, it appears that they also intended to deceive the CPA. Thus, the CPA’s testimony, to the extent that it relies on the Petitioner’s business records and the representations of Petitioner’s employees, can be given little weight.

This is not intended to impugn the CPA’s truthfulness or veracity. It appears that the CPA accepts a good portion of what he was told by his client. It also appears that he accepts the documents that his client provided to him. This is not to say that the CPA does not exercise a certain degree of independent judgment, but his judgment is based on an evidentiary foundation provided by his client. Given that the Petitioner’s employees are not believable and that the Petitioner’s records and the information contained therein is suspect, the CPA’s testimony is insufficient to overcome these problems.

CONSUMERS' SALES AND SERVICE TAX

As verification of the sales of which the Petitioner contends it was required to pay consumers' sales and service tax, the Tax Commissioner's auditors were presented the Petitioner's monthly sales summaries. While the Tax Commissioner's witness, Ms. A, did not expressly so testify, it appears that she and Ms. B suspected that the Petitioner was not correctly or accurately reporting all of its sales. The Tax Commissioner's auditors believed the sales summaries were suspect for two reasons. First, they observed the Petitioner not ringing up all sales on its cash register.⁵ Second, they discovered that the Petitioner did not have daily cash register tapes or "Z" tapes to document its daily sales, which could verify its monthly sales summaries. Having determined that the Petitioner did not produce or maintain a record of all of its retail sales, the Tax Commissioner's auditors conducted their own survey to attempt to verify the Petitioner's monthly sales summaries. The result was that they determined that the Petitioner was under reporting its sales.⁶

The Petitioner takes issue with the auditors' methodology. It attempted to counter the State Tax Commissioner's evidence by presenting evidence that the auditors' methodology was incorrect. It criticizes the auditors' methodology because it was based on a single day's survey. It criticized the auditors for not attempting to determine the Petitioner's sales based on the cost of goods sold. It attempted to rebut the methodology with the CPA's testimony that he conducted the same type of survey as that conducted by the Tax Commissioner's auditors. He contrasted the results of his survey with those of the Tax Commissioner's auditors. Although his survey yielded a percentage of credit card/debit card sales similar to that yielded by the Tax

⁵ Since the Petitioner was not using tape in its cash register, ring up sales with the adding machine turned out to be immaterial. However, this was not initially known to the auditors and, therefore, raised their suspicions.

⁶ As set out above, given Petitioner's fraudulent activities, the monthly sales summaries are not considered reliable evidence of its monthly sales.

Commissioner's auditors' survey, he testified that his survey verified the Petitioner's monthly sales summaries. In other words, he believes the Petitioner did not under report its sales.

The CPA also testified that the Petitioner's monthly sales were reasonable for a restaurant of the Petitioner's size located in West Virginia. He testified that the Petitioner's sales increased by a reasonable amount over the years that the restaurant was open. He testified that the auditors' estimate of sales was not reasonable based on the size of the restaurant.

The Petitioner has the burden of proof. W. Va. Code § 11-10A-10(e) [2002]. Stated differently, the Tax Commissioner's assessment is presumed to be correct. Thus, when a taxpayer is assessed, it must prove that the assessment is incorrect. But is not sufficient for the taxpayer to simply show the estimated assessment is incorrect⁷ and then argue that its original position is correct.⁸ As part of its burden of proof, it must present evidence to show the correct amount of tax it believes it owes. Thus, it is part of the Petitioner's burden of proof to show that it correctly reported its sales or, having incorrectly reported its sales, must show the correct amount thereof and provide some credible evidence to support its position. This burden of proof was not satisfied by presentation of evidence of its own methodology, and then contending that its methodology is superior or preferable to that of the State Tax Commissioner. The Petitioner was required to present evidence to show the actual amount of its sales.

The Petitioner showed that the auditors' methodology was not perfect. Each of its criticisms may be well taken. The CPA then testified that he believed the monthly sales summaries were correct. But the problem with the Petitioner's evidence is that it does not present reliable evidence of its actual sales during the audit period. Like the Commissioner's

⁷ A methodology arriving at an estimate is, by its very nature, incorrect. It does not compute an actual amount. It is an attempt to reach reasonable estimate approximating the correct amount.

evidence, the Petitioner's methodology merely arrives at an estimated amount of its sales during the audit period. The Petitioner, in effect, creates a "battle of the methodologies." Given the statutory provision placing the burden of proof on the Petitioner, the Petitioner must lose any "battle of the methodologies." It can only overcome the Commissioner's estimate by providing evidence of its actual sales.

The CPA emphatically advocates that the Petitioner's monthly sales summaries are accurate. The CPA is credible, in that he is not lying and believes what he is testifying to is true. However, his testimony is based on records that are suspect. As the CPA testified, the monthly sales summaries were presented to him by the Petitioner at the end of each month. In effect, the CPA saw only a finished product for which there was no documentary back up. However, the Tax Commissioner presented evidence to show that the Petitioner may have falsified the monthly summaries before they were presented to the CPA. Given the Petitioner's fraudulent actions in other respects, the monthly sales summaries are unreliable. The CPA may believe the monthly summaries are correct, but there is no evidence by which this can be proven.

As more fully discussed above, the Petitioner is done in by its illegal and fraudulent behavior and its failure to create and maintain reasonable business records. This Office finds that the Petitioner's lack of credibility, combined with the lack of evidence respecting the Petitioner's actual retail sales, leads to the conclusion that the Petitioner's sales summaries were, in and of themselves, insufficient to overcome the presumption of correctness of the Tax Commissioner's assessment, to satisfy the Petitioner's burden of proof. The Petitioner would more likely have satisfied its burden of proof had it presented objective, documentary evidence, such as cash register tapes and supporting "Z" tapes, to support its sales summaries. Both the

⁸ This may suffice where the Petitioner presents sufficient credible evidence to show that its original position is, in fact, correct.

absence of these records or other detailed sales records dooms its consumers' sales and service tax petition to failure.

BUSINESS FRANCHISE TAX

The Petitioner's argument with respect to the business franchise tax is based on its arguments respecting the consumers' sales and service tax. The failure of the Petitioner's arguments respecting the consumers' sales and service tax assessment causes its arguments respecting the business franchise tax to fail.

CORPORATION NET INCOME TAX

The Petitioner's argument with respect to the corporation net income tax is based on its arguments respecting the consumers' sales and service tax. The failure of the Petitioner's arguments respecting the consumers' sales and service tax assessment causes its arguments respecting the corporation net income tax to fail.

PURCHASERS' USE TAX

The purchasers' use tax is based on four separate purchases or categories of purchases. Specifically, it is based on the following purchases: 1) Leasehold improvements; 2) Restaurant equipment purchases; 3) Common area maintenance charges; and 4) Miscellaneous purchases.

The auditors picked up a purchase of \$_____ which involved improvements its leasehold premises. The purchase was picked up from an asset depreciation schedule. With its memorandum of law, the Petitioner submitted a two page invoice dated approximately the same time showing the purchase and installation of improvements to its leasehold premises. The invoice shows purchases of \$_____. The invoice also shows that the Petitioner paid consumers' sales and service tax of \$_____. This Office is convinced that the invoice is for the

purchase picked up by the auditors. Since consumers' sales and service tax was paid on the invoice, the purchasers' use tax attributable to that purchase must be abated.⁹

The Petitioner also challenges the common area maintenance charge. This charge is a separately stated charge for the maintenance of common areas in the plaza where the Petitioner's restaurant is located. The Petitioner contends that the charge for common area maintenance is part of its lease payment for the premises and, as such, is exempt from consumers' sales and service tax and, therefore, the purchasers' use tax.

This argument is without merit. The charge is for services provided by the landlord to all of the tenants of the plaza, for which the Petitioner pays its proportionate share. The key is that the charge is for services, not rent for all or some portion of the leasehold premises. Thus, the charge is presumed to be taxable, unless shown to be exempt. There has been no such showing. Therefore, the charge is taxable.

The other item challenged by the Petitioner consists of miscellaneous purchases. The purchases include bleach, oven cleaner, takeout boxes, foil, wax paper, soap, film, towels, toilet tissue, trash can liners, and other similar items. The Petitioner contends that these purchases were used in the preparation of food sold to customers and that, therefore, they should be exempt.

The Petitioner's argument is without merit. The purchases would be exempt if they were resold to customers. This would include items provided to customers as part of the provision of food, such as napkins or straws. It would also include takeout boxes. However, a listing of the items in the audit work papers does not disclose that takeout boxes or other items provided to

⁹ The amount picked up was \$ _____, less than the actual invoice. Therefore, the tax on the lesser amount will be abated.

customers were picked up by the auditors. Instead, the items picked up are used and consumed in the Petitioner's business. As such, they are taxable.

PERSONAL INCOME TAX WITHHOLDING

As with the other taxes, the Petitioner bears the burden of proving that the assessment is incorrect. As discussed above, it must provide evidence of the amount of withholding tax that it actually owes. As with the consumers' sales and service tax, the Petitioner contends that the amount of withholding that it reported and paid is correct.

The Petitioner contends that the auditors' methodology is incorrect. In the CPA's words, it is "impossible." It then asserts that it reported all of the wages and paid and the withholding thereon. There are several problems with the Petitioner's assertion. First, the withholding summary contains admitted fraud. Second, the Petitioner may not prevail by merely asserting that the auditors' methodology is wrong. Third, the summaries submitted by the Petitioner are simply not reasonable.

As previously discussed, the W-2 summaries submitted by the Petitioner are based, in part, on the Petitioner's most obvious fraudulent act. Each W-2 summary contains a W-2 for Mr. C and does not contain one for Mr. D. This is because, as the CPA testified, the Petitioner was paying Mr. D's wages to Mr. C. This was clearly illegal and was clearly for some fraudulent purpose. Yet the Petitioner asks this Office to disregard this fraud, assume that the W-2 was filed in the name of Mr. D, and believe that the rest of the W-2 summary is true and accurate. The Petitioner asks too much. This fraud taints the rest of this document to a greater degree than the remainder of the Petitioner's evidence. This document is not to be believed.

As more fully set out above, it is not enough that the Petitioner assert that the methodology on which the assessment is based is wrong. It must show that it was correct in

reporting and paying its tax. It does not do so. Where are its daily or weekly work schedules? Where are the periodic time records showing the hours its employees worked? Where are copies of records showing how it computed its employees' gross and net pay? Do they exist? Because of Petitioner's fraudulent activities, it is believed that there is some fraudulent purpose in the Petitioner's failure to prepare and retain such documents.

Other evidence that the Petitioner's W-2 summaries are inaccurate is that they do not withstand scrutiny when analyzed on an hourly wage basis. The Petitioner's restaurant is open approximately 4500 hours per year (five 13-hour days plus one 11.5-hour day plus one 13.5-hour day equals 90 hours per week times 50 weeks per year¹⁰). In 2005, the year in which the Petitioner's total reported payroll was \$_____, its average hourly payroll for the hours it was open for the entire year was just over \$6.55 per hour (\$_____ divided by 4500 equals \$6.5523). This is the average hourly wage for all of its employees working in any given hour, not an hourly wage per employee. The CPA testified that the Petitioner had at least six employees working when he was there (a manager, two waiters/waitresses, a busboy and two kitchen workers), which seems like a bare minimum necessary to proper operation of the restaurant. Using this assumption, the Petitioner's employees averaged \$1.11 per hour for the entire year. Ms. A testified that she saw nine employees working. If she is correct, then the employees averaged \$.74 per hour. In 2003, when the Petitioner's reported payroll was \$_____, the hourly wage for all employees was just under \$8.64 per hour. If the Petitioner average six workers at a time, then those employees averaged just under \$1.44 per hour for the entire year. If Ms. A is correct, and the Petitioner used nine employees, then the Petitioner's

¹⁰ The auditors assumed the restaurant was closed 6 days per year. This calculation assumes it was closed 14 days per year. This does not include any hours worked by employees for preparation prior to opening or for clean up after closing.

employees averaged just under \$.96 per hour. These figures demonstrate that the total wages paid to the Petitioner's employees, as shown on the W-2 summary, is simply not realistic. This calculation demonstrates that this document appears to be fraudulent for a reason other than the C/D wage fraud. It is reasonable to assume that some of the Petitioner's employees were being paid under the table.

The Petitioner contends that the auditors' calculation of total wages is too high. This assertion may be correct. On the other hand, its reported wages appear to be too low. The answer probably lies somewhere in the middle. But it is the burden of the Petitioner, not the State Tax Commissioner, to show the correct wages paid. Employee work schedules, time cards, calculations of gross and net wages and other documentation might help prove the Petitioner's case. However, in the absence of credible proof of the wages paid, the Petitioner has failed to satisfy its burden of proof.

CONCLUSIONS OF LAW

Based upon all of the above it is **DETERMINED** that:

1. In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is on the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code § 11-10A-10(e) [2002]; W. Va. Code. St. R. §§ 121-1-63.1 and 69.2 (Apr. 20, 2003).

2. Where an assessment is based on a methodology developed to estimate the amount of tax due, to satisfy its burden of proving that against the assessment is erroneous a taxpayer may not merely demonstrate that the estimated assessment is incorrect, but must provide credible evidence to show the actual amount of tax due.

3. Intentional illegal or fraudulent conduct by a taxpayer or its principals, agents or employees with respect to a transaction pertaining to one tax may impugn the credibility of the taxpayer or its principals, agents or employees with respect to other transactions or other taxes.

4. The Petitioner failed to satisfy its burden of proof by reason of its failure to provide evidence to show the actual amount of its sales subject to the consumers' sales and service tax.

5. Where a business franchise tax assessment is derivative of a consumers' sales and service tax assessment against the taxpayer, the failure of the taxpayer to satisfy its burden of proof with respect to the consumers' sales and service tax constitutes a failure of its burden of proof with respect to the business franchise tax.

6. Where a corporation net income tax assessment is derivative of a consumers' sales and service tax assessment against the taxpayer, the failure of the taxpayer to satisfy its burden of proof with respect to the consumers' sales and service tax constitutes a failure of its burden of proof with respect to the corporation net income tax.

7. Presentation of an invoice showing that a taxpayer paid consumers' sales and service tax with respect to a single purchase will relieve said taxpayer of a purchasers' use tax assessment with respect to said purchase.

8. A common area maintenance provision in a lease involves a charge for the provision of services, as opposed to rent for the leasehold interest and, as such, is subject to purchasers' use tax absent some evidence that the services provided are otherwise exempt.

9. Items purchased by a taxpayer and used or consumed in its business are subject to the purchasers' use tax.

10. The intentional illegal or fraudulent activity by a taxpayer or its principals, agents or employees, such as filing a W-2 that shows that one employee received another employee's income, may impugn the validity of all transactions engaged in by that taxpayer.

11. Where an assessment is based on a methodology developed to estimate the amount of tax due, to satisfy its burden of proving that against the assessment is erroneous a taxpayer may not merely demonstrate that the estimated assessment is incorrect, but must provide credible evidence to show the actual amount of tax due.

12. The Petitioner failed to satisfy its burden of proof by reason of its failure to provided sufficient evidence to show the actual wages paid to its employees and the amount of personal income tax withheld from such wages and paid to the State of West Virginia.

DISPOSITION

WHEREFORE, it is the **FINAL DECISION** of the **WEST VIRGINIA OFFICE OF TAX APPEALS** that the consumers' sales and service tax assessment issued against the Petitioner for the period of January 1, 2003, through January 31, 2006, for tax in the amount of \$_____, interest in the amount of \$_____, updated through August 31, 2006, and additions to tax in the amount of \$_____, totaling \$_____, should be and is hereby **AFFIRMED**.

Interest continues to accrue on this unpaid tax until this liability is fully paid.

It is **ALSO** the **FINAL DECISION** of the **WEST VIRGINIA OFFICE OF TAX APPEALS** that the business franchise tax assessment issued against the Petitioner for the period of January 1, 2003, through December 31, 2005, for tax in the amount of \$_____, interest in the amount of \$_____, computed through August 31, 2006, and additions to tax in the amount of \$_____, totaling \$_____, should be and is hereby **AFFIRMED**.

Interest continues to accrue on this unpaid tax until this liability is fully paid.

It is **ALSO** the **FINAL DECISION** of the **WEST VIRGINIA OFFICE OF TAX APPEALS** that the corporation net income tax assessment issued against the Petitioner for the period of January 1, 2003, through December 31, 2005, for tax in the amount of tax in the amount of \$_____, interest in the amount of \$_____, computed through August 31, 2006, and additions to tax in the amount of \$_____, totaling \$_____, should be and is hereby **AFFIRMED**.

Interest continues to accrue on this unpaid tax until this liability is fully paid.

It is **ALSO** the **FINAL DECISION** of the **WEST VIRGINIA OFFICE OF TAX APPEALS** that the purchasers' use tax assessment issued against the Petitioner for the period of October 1, 2001, through March 31, 2006, for tax in the amount of tax in the amount of \$_____, and interest in the amount of \$_____, computed through August 31, 2006, totaling \$_____, should be and is hereby **MODIFIED** in accordance with the above Conclusions of Law for **revised tax** in the amount of \$_____.

Because the purchasers' use tax has been modified it is necessary to compute the amount of interest on the revised purchasers' use tax due. This Office will require the State Tax Commissioner to compute the amount of interest due on the revised tax and submit the same to the Petitioner for review, within fifteen (15) days of receipt of this decision. Upon review, if the Petitioner agrees with the State Tax Commissioner's revised interest computation, Petitioner's counsel will notify both this Office and counsel for the State Tax Commissioner. If the Petitioner disagrees with the Tax Commissioner's computation, then within ten (10) days the parties are to confer in an attempt to reach an agreed upon interest computation. If, at that time, the parties are unable agree upon a computation of interest, each party shall submit a detailed computation of interest to this Office, with an explanation of why its computation is correct and

the opposing party's computation is incorrect. Based on those statements, this Office will render a decision as to the correct computation of interest on the purchasers' use tax assessment.

Interest continues to accrue on the unpaid tax until this liability is fully paid.

It is **ALSO** the **FINAL DECISION** of the **WEST VIRGINIA OFFICE OF TAX APPEALS** that the personal income withholding tax assessment issued against the Petitioner for the period of January 1, 2003, through December 31, 2005, for tax in the amount of \$_____, interest in the amount of \$_____, computed through August 31, 2006, and additions to tax in the amount of \$_____, totaling \$_____, should be and is hereby **AFFIRMED**.

Interest continues to accrue on this unpaid tax until this liability is fully paid.