

**ST 01-5**

**Tax Type: Sales Tax**

**Issue: Unreported/Underreported Receipts (Non-Fraudulent)**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS**

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**THE DEPARTMENT OF REVENUE  
OF THE STATE OF ILLINOIS,**

v.

**DOE'S LIQUOR &  
DELICATESSEN,  
Taxpayer**

No. 99-ST-0000  
IBT# 0000-0000  
NTL 00 0000000000000000  
Periods: 1/1/94 to 12/31/97  
Denial of Refund Claim  
Periods: 1/1/91 to 12/31/93

**Ted Sherrod  
Administrative Law Judge**

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**RECOMMENDATION FOR DISPOSITION**

**Appearances:** Alan M. Depcik, Esq. for Doe's Liquor & Delicatessen; Gary Stutland, Esq., Special Assistant Attorney General, for the Illinois Department of Revenue.

**Synopsis:**

This matter comes on for hearing pursuant to timely protests of Notice of Tax Liability No. 00 0000000000000000 covering tax periods 1/1/94 to 12/31/97, and a Notice of Tentative Denial of Claim issued on August 11, 1999 covering tax periods 1/1/91 to 12/31/93. At issue is whether the taxpayer underreported his receipts for the audit period of January 1, 1994 to December 31, 1997, and whether the taxpayer is entitled to a credit for overpayment of taxes for the tax periods January 1, 1991 to December 31, 1993. Following the submission of all evidence and a review of the record, it is recommended

that this matter be resolved in favor of the Department. In support of this recommendation, I make the following findings of fact and conclusions of law.

**Findings of Fact:**

1. The Department's *prima facie* case, inclusive of all jurisdictional elements, was established by the admission into evidence of the SC-10-K, Audit Correction and/or Determination of Tax Due (herein "correction of returns"), the Notice of Tax Liability ("NTL") showing a proposed liability in the amount of \$23,861 for the tax periods 1/1/94 to 12/31/97, and the Notice of Tentative Denial of Claim for the tax periods 1/1/91 to 12/31/93. Dept. Ex. 1, 2. <sup>1</sup>
2. The taxpayer is a food, liquor and import goods retailer located at 123 Alphabet Lane, Anywhere, Illinois. Tr. p. 29; Dept. Ex. 1.
3. The taxpayer is an unincorporated sole proprietorship owned by John Doe (hereinafter "Doe"). Tr. pp. 70, 89; Dept. Ex. 1.
4. The Department audited the taxpayer for the taxable periods of January 1, 1994 to December 31, 1997. Tr. pp. 6, 17, 18, 63; Dept. Ex. 1.
5. During the audit, the auditor requested Retailers' Occupation Tax returns, Federal and Illinois income tax returns, a general ledger, purchase and/or disbursement journals, sales journals, general journals, bank statements, invoices and register tapes. Tr. pp. 20, 21, 29, 30, 68; Dept. Ex. 1.
6. The taxpayer's books and records were incomplete, and the Department's auditor was not supplied with daily sales sheets, a general ledger or any sales journals, sales invoices or general journals, and with incomplete invoices, register tapes, purchase

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<sup>1</sup> Unless otherwise noted, findings of fact apply to the tax periods.

and disbursement journals and bank statements. Tr. pp. 28, 29, 34, 36, 37, 49, 67, 68, 89, 90, 92, 93, 107, 108, 109.

7. The taxpayer did not keep a general ledger or complete purchase and disbursement journals. Tr. pp. 89, 90.
8. The taxpayer did not maintain daily sales sheets or a complete set of cash register tapes and other data providing a daily record of the gross amount of sales as required by the Department's rules and regulations. Tr. pp. 28, 49, 50.
9. Notwithstanding the taxpayer's failure to maintain complete books and records, the Department's auditor obtained, either from the taxpayer or through her own efforts, the following books and records: the taxpayer's retailers' occupation tax returns for all tax periods under audit, the taxpayer's Federal and Illinois income tax returns for 1994, 1995 and 1996, bank statements for two accounts for the years 1994 and 1995, a check register setting forth the names of the taxpayer's suppliers, and incomplete bank statements, purchase and sales invoices, register tapes and purchase and disbursement journals. Tr. pp. 23, 24, 30, 49, 67, 68, 92, 93, 108, 109; Dept. Ex. 1.
10. Doe did not deposit all of the cash the taxpayer realized from its business into the taxpayer's bank account; this determination was made by comparing gross receipts shown on the taxpayer's tax returns to funds deposited into the taxpayer's bank accounts. Tr. p. 25; Dept. Ex. 1.
11. The auditor could not substantiate the sales reported by the taxpayer on its retailers' occupation tax returns because the taxpayer did not maintain daily sales sheets or a complete set of register tapes. Tr. pp. 28, 109.

- 12.** Gross receipts shown on the taxpayer's sales tax returns differed from gross receipts shown on the taxpayer's books and Federal income tax returns. Tr. pp. 25, 26, 27; Dept. Ex. 1.
- 13.** Purchases of merchandise by the taxpayer taxed at the sales tax rate of 8.75% exceeded sales of such merchandise reported for 1995 and 1996; this determination was based upon a survey of the taxpayer's suppliers as shown by the taxpayer's check register for 1994, 1995 and 1996. Tr. pp. 30, 31, 32, 34, 35, 36; Dept. Ex. 1.
- 14.** Since the taxpayer tendered incomplete books and records for inspection by the auditor, the Department was required to estimate the taxpayer's gross receipts based primarily upon information contained in the taxpayer's federal income tax returns to arrive at a reasonable approximation of the taxpayer's gross receipts. pp. 37, 38, 39, 40, 41, 42, 43.
- 15.** The auditor determined the taxpayer's gross receipts by including gross receipts reported by the taxpayer, and attributing additional gross receipts to the taxpayer to the extent expenses evidenced by the taxpayer's Federal income tax returns or other sources exceeded income reported on these returns. Tr. pp. 37, 38, 39, 40, 41, 42, 43; Dept. Ex. 1.
- 16.** The auditor attributed additional gross receipts to the taxpayer for 1995 to the extent gross receipts reported on the taxpayer's Federal income tax return were not reported on the taxpayer's retailers' occupation tax returns, and made an adjustment attributing additional receipts based upon an increase in the taxpayer's investments. Tr. pp. 40, 41; Dept. Ex. 1.

17. The auditor adjusted underreported gross receipts to exclude sales taxes and to allocate receipts to each month of the audit period. Tr. pp. 41, 42.
18. The taxpayer underreported gross receipts from sales of merchandise taxable at 8.75%, but did not underreport sales of food taxable at 2%; consequently, all underreported receipts were taxed at 8.75%. Tr. pp. 109, 110; Dept. Ex. 1.
19. The taxpayer's Federal income tax return for 1997 was not available at the time of the audit; consequently, the deficiency assessed for 1997 was based upon a projection determined by averaging the liability determined for 1994, 1995 and 1996. Tr. pp. 23, 38, 49.

**Conclusions of Law:**

The issues to be decided in this case are whether the taxpayer underreported its receipts for the audit period January 1, 1994 through December 31, 1997, and whether the taxpayer's claim for credit covering the tax periods January 1, 1991 through December 31, 1993 was properly denied. With respect to the underreported receipts issue, the correction of returns submitted as part of the Department's Exhibit 1 is *prima facie* correct and constitutes *prima facie* evidence of the correctness of the amount of tax shown to be due thereon. 35 ILCS 120/4; Filichio v. Department of Revenue, 15 Ill. 2<sup>nd</sup> 327 (1958). In order to overcome the presumption of validity attached to the Department's corrected returns the taxpayer must produce competent evidence, identified with its books and records showing that the Department's returns are incorrect. Copilevitz v. Department of Revenue, 41 Ill. 2<sup>nd</sup> 154 (1968); Central Furniture Mart v. Johnson, 157 Ill. App. 3<sup>rd</sup> 907 (1<sup>st</sup> Dist. 1987); Masini v. Department of Revenue, 60 Ill. App. 3<sup>rd</sup> 11 (1<sup>st</sup> Dist. 1978).

The Retailers' Occupation Tax Act ("ROTA") has a specific requirement for maintaining books and records, which provides:

Every person engaged in the business of selling tangible personal property at retail in this State shall keep records and books of all sales of tangible personal property, together with invoices, bills of lading, sales records, copies of bills of sale, inventories prepared as of December 31 of each year or otherwise annually as has been the custom in the specific trade and other pertinent papers and documents.

35 ILCS 120/7.

A taxpayer's duty to keep such books and records is mandatory. Smith v. Department of Revenue, 143 Ill. App. 3<sup>rd</sup> 607 (5<sup>th</sup> Dist. 1986); Mel-Park Drugs, Inc. v. Department of Revenue, 218 Ill. App. 3<sup>rd</sup> 203 (1<sup>st</sup> Dist. 1991). If a taxpayer does not have adequate books and records to support its monthly tax returns the Department may use its best judgment to estimate the taxpayer's gross receipts and is justified in going outside the taxpayer's books and records to obtain information to correct the taxpayer's returns. Young v. Hulman, 39 Ill. 2<sup>nd</sup> 219 (1968); Mel-Park Drugs, Inc. v. Department of Revenue, *supra*. The method used by the Department in such a case must only meet a minimal standard of reasonableness. Mel-Park Drugs, Inc., 218 Ill. App. 3<sup>rd</sup> at 207; Smith, 143 Ill. App. 3<sup>rd</sup> at 611. The Department meets a minimal standard of reasonableness if it uses the best information it has available and makes fair assumptions. *Id* at 611.

In this case, the Department's auditor was not supplied with daily sales sheets, a general ledger, sales journals, sales invoices, or general journals. Tr. pp. 28, 49, 89, 92, 107. The auditor was also supplied with incomplete purchase invoices, register tapes, purchase and disbursement journals and bank statements. Tr. pp. 29, 49, 67, 68, 92, 93,

106, 107, 108, 109. Because the taxpayer did not maintain a general ledger or complete purchase and disbursement journals, or maintain daily sales sheets or a complete set of cash register tapes, it did not comply with record keeping requirements mandated by 35 **ILCS** 120/7; see also 86 Ill. Admin. Code § 130.805 which elaborates upon the books and records that the taxpayer is required to maintain to be in compliance with the ROTA. Since the taxpayer failed to perform its statutory duty to keep adequate books and records regarding its retailers' occupation taxes, the Department was permitted to look outside of the taxpayer's books and records to obtain information to correct the taxpayer's returns. Smith v. Department of Revenue, *supra*; Young v. Hulman, *supra*; Mel-Park Drugs, Inc. v. Department of Revenue, *supra*.

The auditor testified that she arrived at the taxpayer's gross receipts for 1994, 1995 and 1996 by attributing gross receipts to the taxpayer to the extent expenses evidenced by the taxpayer's Federal income tax returns and other sources exceeded income reported on the taxpayer's Federal income tax returns. Tr. pp. 37, 38, 39, 40, 41, 42, 43. She also attributed gross receipts to the taxpayer for 1995 to the extent receipts reported on the taxpayer's Federal income tax return were not included in the taxpayer's ROTA returns, and made an adjustment attributing additional receipts based upon an increase in the taxpayer's investments. Tr. pp. 40, 41. The auditor also made adjustments to exclude sales taxes from underreported receipts and determine underreported receipts by month. Tr. pp. 41, 42.

Since the auditor conceded the accuracy of the taxpayer's report of food sales taxable at 2%, she attributed all of the underreported receipts to sales of merchandise taxable at 8.75%. Tr. p. 110. This would appear to be appropriate given the evidence in

the record that high rate merchandise was improperly reported. Tr. pp. 12, 30, 31, 32, 34, 35, 36; Dept. Ex. 1. Since the taxpayer's Federal income tax return for 1997 was not available, the auditor projected gross receipts for 1997 based upon her findings for 1994, 1995 and 1996. Tr. pp. 23, 38, 49.

The auditor's testimony established that the Department determined underreported receipts by using the best information it had available and making fair and reasonable assumptions. Given the taxpayer's failure to maintain required books and records, I find that the methods used met the standard of reasonableness necessary to sustain the Department's determinations. Smith v. Department of Revenue, *supra*.

The taxpayer contends that the audit should have taken into account funds from outside depositors who gave money to Doe for safekeeping rather than putting these funds in a bank. Tr. pp. 9, 128. During the hearing the taxpayer attempted to support this contention through testimony of Doe and his accountant (Tr. pp. 71, 72, 73, 74, 75, 76, 77, 78, 95, 96, 97), and through affidavits of purported depositors. However, I find it highly improbable that Doe would have been allowed to use funds given him for safekeeping for his own benefit without the depositors' knowledge, or that depositors would have given him funds without knowing what he intended to do with their money. Consequently, I have given no weight to the testimony regarding the receipt of these funds. Moreover, the affidavits of purported depositors were not admitted into the record and have not been accorded any weight by this tribunal.

There is also testimony regarding amended returns and additional sales records that may have been available during the audit for use in arriving at a more accurate estimate of the taxpayer's gross receipts. Tr. pp. 44, 45, 46, 48, 49, 50, 92, 93. However,

none of these documents were offered as exhibits at the hearing. Therefore, I do not know what information may have been contained in them. Nor is there any competent or credible evidence that whatever information might have been disclosed by these documents would have better reflected the taxpayer's gross receipts than the information that was used by the auditor.

A taxpayer cannot overcome the Department's *prima facie* case merely by denying the accuracy of the Department's determination. Central Furniture v. Johnson, *supra*. Simply questioning the Department's assessment or denying its accuracy is not enough. Quincy Trading Post v. Department of Revenue, 12 Ill. App. 3<sup>rd</sup> 725 (4<sup>th</sup> Dist. 1973). A taxpayer can overcome the Department's *prima facie* case only by providing competent evidence identified with the taxpayer's books and records. Copilevitz v. Department of Revenue, *supra*; Central Furniture Mart v. Johnson, *supra*; Masini v. Department of Revenue, *supra*; Vitale v. Department of Revenue, 118 Ill. App. 3<sup>rd</sup> 210 (3<sup>rd</sup> Dist. 1983). Moreover, mere oral argument without some documentary evidence to substantiate the taxpayer's claim that the *prima facie* case was prepared incorrectly is not sufficient. Quincy Trading Post v. Department of Revenue, *supra*; Mel-Park Drugs, Inc. v. Department of Revenue, *supra*. In the instant case, the taxpayer has presented no documentary evidence whatsoever to show that the Department's determination was arbitrary, capricious or unreasonable. Because the taxpayer has not produced any documentary evidence identified with its books and records to support its claim that the audit methods used by the Department were not the best methods to determine the taxpayer's liability, the Department's *prima facie* case stands unrebutted. Copilevitz v. Department of Revenue, *supra*, Central Furniture Mart v. Johnson, *supra*, Masini v.

Department of Revenue, supra, Quincy Trading Post v. Department of Revenue, supra; Mel-Park Drugs, Inc. v. Department of Revenue, supra. Accordingly, I find that the taxpayer has not provided sufficient evidence to overcome the Department's *prima facie* case.

With respect to the taxpayer's claim for credit, the Department's Notice of Tentative Claim Denial, submitted as the Department's Exhibit 2, constitutes *prima facie* proof of the correctness of the Department's determination, as shown therein. 35 ILCS 120/6b. Once the Department has established its *prima facie* case, the burden shifts to the claimant to overcome this presumption of validity. Sprague v. Johnson, 195 Ill. App. 3<sup>rd</sup> 798 (4<sup>th</sup> Dist. 1990); Clark Oil & Refining Corp. v. Johnson, 154 Ill. App. 3<sup>rd</sup> 773 (1<sup>st</sup> Dist. 1987); Central Furniture Mart, Inc. v. Johnson, supra. As noted previously, to overcome the Department's *prima facie* case the taxpayer must present consistent, probable evidence identified with its books and records and showing that the Department's determination is incorrect. Copilevitz v. Department of Revenue, supra; Central Furniture Mart v. Johnson, supra; Masini v. Department of Revenue, supra.

While the taxpayer alleges that he paid tax on sales of food at the 8.75% rate rather than the 2% rate applicable to food during the tax periods 1/1/91 to 12/31/93 (Tr. pp. 78, 79, 80, 81), the taxpayer submitted no documentary evidence to support this claim. Oral testimony without corroborating books and records is insufficient to overcome the Department's *prima facie* case. Mel-Park Drugs v. Department of Revenue, supra; Quincy Trading Post v. Department of Revenue, supra. Consequently, unsubstantiated oral testimony based on Doe's recollections, the only evidence provided

in support of the taxpayer's claim, is not sufficient to rebut the Department's *prima facie* case. *Id.*

**WHEREFORE**, for the reasons stated above, it is my recommendation that NTL 00 0000000000000000, for the periods 1/1/94 to 12/31/97, be affirmed in its entirety and that the Department's denial of the taxpayer's claim for credit for the periods 1/1/91 to 12/31/93 be upheld.

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Ted Sherrod  
Administrative Law Judge

Date: January 25, 2001