

THE BUSINESS REVIEW

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In the big picture, New York may be open for business

But nitty gritty issues—like sales tax audits—continue to haunt many industries

BY ADAM SICHKO
THE BUSINESS REVIEW

Mario and Elda Abate laid off a quarter of their staff at Elda's on Lark in 2010, facing a tax bill they definitely didn't have the cash flow to cover.

The Abates cut the three workers to build a cushion of cash flow—after a state auditor probed sales-tax records from as far back as 2004.

The tax audit provides a window into the type of interaction with state agencies that tests whether New York is truly “open for business,” as Gov. Andrew Cuomo often says.

For a week, Elda Abate devoted her typical 5 p.m.-to-5 a.m. shift at the restaurant to culling month-by-month records of her sales from her computerized system—seeking to justify her tax payments.

According to Abate, the auditor ignored that and instead assessed a much higher tax bill with penalties and interest. To Abate, she was guilty, unless she could prove otherwise to someone she judged to have no grasp of her business model.

“Nobody should experience what we went through, especially small, family-owned businesses. They are the pillar of the state,” Abate said.

“It was insane. They scare you. It kills your spirit,” Abate said. “People and businesses are leaving New York every day. Why are we giving them more reasons?”

That resentment cuts to the heart of New York's notorious business climate.

Cuomo points to big-picture action when arguing why New York is now “open for business”: a balanced budget; a cap that limits tax increases; handing out \$200 million of new economic development money.



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THE BUSINESS REVIEW

A state sales tax audit of Elda's on Lark led to layoffs at the Albany restaurant. “Nobody should experience what we went through, especially small, family-owned businesses. They are the pillar of the state,” says owner Elda Abate.

BELOW: Elda's is a fixture on Albany's Lark Street—and a quick walk to the state Capitol building.

Reforming audits of sales taxes? Nitty-gritty stuff—but much more important in the eyes of business lobbies.

“Addressing that will do far more than what the regional economic development councils or the tax cap will do today, in terms of creating jobs,” said Michael Durant, state director of the National Federation of Independent Business.

“These are the things holding employers back from hiring. It is less splashy, but it has more impact,” Durant said. “The state really does have a stigma that they're always out to get business. It's dubious, but they've earned it.”

The NFIB, which represents 10,000 small businesses, was livid over how far back the tax department was digging in its audits—and the ways auditors decided how much unpaid sales tax a business allegedly owed.

Former Gov. David Paterson ordered the tax department to hire more than 330 new staff in the audit division in 2010, after adding 180 others in the prior year. The new staff was to come up with \$220 million of revenue to ease the state's budget pains.

State officials said the audits were motivated, in part, by a desire to root out businesses gaining an edge over their competition by skimming on taxes.

At NFIB's request, investigators for state



Comptroller Thomas DiNapoli probed the tax department's audit practices.

Last month, DiNapoli's team released a final report after 18 months of work. The four-page document found no wrongdoing and contradicted key claims business owners and lobbies had been making about audits and the people conducting them.

TAX: New comptroller report took no issue with the way the state handled the audits



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State Comptroller Thomas DiNapoli recently issued a report on the tax department's audit practices. Conclusion: No wrongdoing on the state's part.

Vendors collect sales taxes on behalf of the state, and must forward them on every month or quarter. William Comiskey, the state's former top tax enforcement official, said too many vendors treat the money like a free loan.

"A lot of vendors wouldn't want to give up the float," Comiskey said. "By not fixing this, the state is complicit."

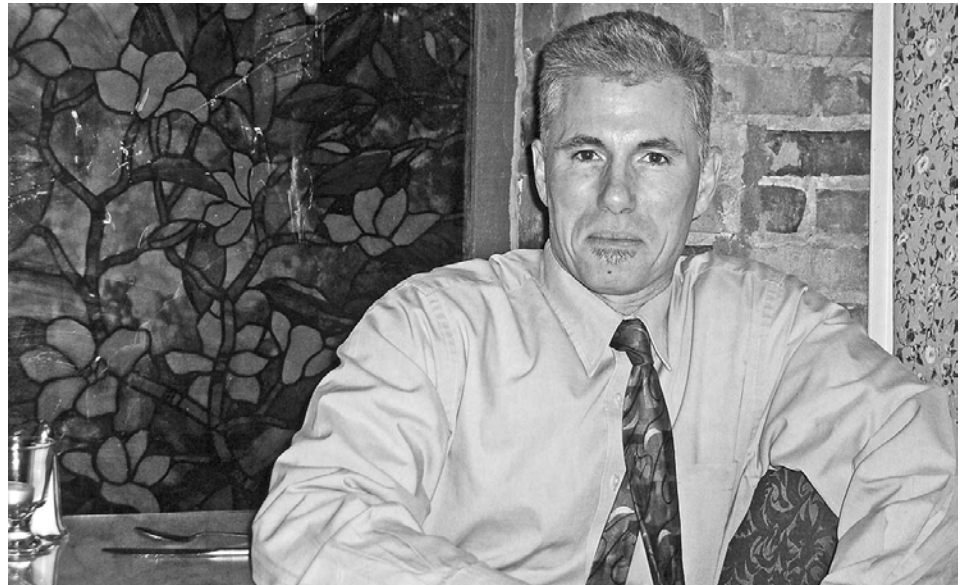
Restaurant audits alone doubled in 2010, to 1,300, and those weren't the only small businesses affected. Bars, convenience stores, jewelers and small construction firms also faced audits, CPAs said.

Auditors, by law, can estimate a sales tax bill if they determine "adequate" business records do not exist. Auditors can do this by observing a business for a day and extrapolating that data, or by applying industry-wide statistics to a specific business.

"It's no wonder there are sparks flying in every direction. It's too much, too late," said Comiskey, who left the state in late 2010 and joined the Albany office of law firm **Hodgson Russ**.

"Auditors have every right to look. But you can see how that would strangle anyone trying to stay in business, pay the bills, make a little money," Comiskey said.

"People say, 'Do I pay my staff, or take this money and put it aside like I'm required to do?' Salt-of-the-Earth people end up committing what is a felony," Comiskey added: "I now have a lot more empathy than perhaps I once had with businesses and the pressure they're under."



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Thom Wallace, who owned the former Olde Shaker Inn in Latham, fought a five-figure tax bill and won. He says the state's treatment of businesses can deter people from opening shop.

On the web

How did we get here? Read past coverage of the tax audit issue at

tinyurl.com/BizReviewAudits

Since DiNapoli's audit began, a new administration took office. Sales tax audits continue at about the same pace—roughly 33,000 a year—but the department has made changes, said spokesman Edward Walsh.

Supervisors now have more direct oversight of audits, and they continue expanding educational materials about audits, Walsh said. Cuomo is building a panel to recommend tax reforms, including in the area of sales taxes, Walsh said.

"We understand some owners go into business because they are passionate about the opportunity to commercialize ... and not necessarily the opportunity to learn accounting and compliance requirements," Walsh said. "While we recognize business operators may find this challenging, we do have an obligation to enforce the tax code."

In interviews, CPAs said the sales tax audits appear to have died down. But problems still exist.

"It does not make someone want to open a business and be subjected to that treatment," said Thom Wallace, former owner of the Olde Shaker Inn, a restaurant in Latham.

Wallace spent \$5,000 fighting a five-figure tax bill. He said he wound up owing nothing. For other reasons, Wallace said, he closed the restaurant in 2011. He is now looking to

Facts & figures

Inside the state tax department

37,500 Sales tax audits the state conducted in its 2009-10 fiscal year

\$1 billion Tax bills resulting from those audits

2,300 Employees in the audit/enforcement division

Source: Office of the State Comptroller; state Division of the Budget

follow his mother, his siblings and his son by moving to the South.

"The numbers were so unreasonably unrealistic. It was like, 'Let's Make A Deal,'" Wallace said. "It was a failed money grab.

"They have every right to audit," Wallace added. "But their approach is, 'prove us wrong.' Uh, aren't you supposed to prove to me that you are right?"

Elda Abate has rehired two of the three people she laid off from her Lark Street restaurant as her audit began. She settled her case with the state in spring 2011. She declined to say what she paid, or what they said she owed.

Abate charged the settlement on her credit card.

"That is not the way you should do business. But we wanted it over with," she said. "We are very honest. We work very hard. How do they expect small businesses to handle this?"