

**ST 09-2**  
**Tax Type: Sales Tax**  
**Issue: Books And Records Insufficient**

**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.

**ABC LEASING SALES, INC.,  
Taxpayer**

**No. 06-ST-0000**  
**IBT# 0000-0000**  
**NTL# 00 0000000000000000 -**  
**00 0000000000000000**

**Ted Sherrod**  
**Administrative Law Judge**

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**RECOMMENDATION FOR DISPOSITION**

**Appearances:** Special Assistant Attorney General George Foster on behalf of the Illinois Department of Revenue; Harry W. Rubinoff of Law Offices of Harry W. Rubinoff on behalf of ABC Leasing Sales, Inc.

**Synopsis:**

The Department of Revenue (“Department”) conducted an audit of ABC Leasing Sales, Inc. (“taxpayer”) for the period December 1998 through March 2005. During the audit, the taxpayer did not provide the auditor with any books and records, and the auditor estimated the amount of liability owed by the taxpayer based upon a summary of an investigation of the taxpayer conducted by the Federal Bureau of Investigation covering the audit period. An evidentiary hearing was held on October 15, 2008 during

which the taxpayer argued that the audit was improperly conducted and that the Notices of Tax Liability at issue, based on the auditor's audit determinations, should be set aside. After reviewing the testimony and the documents of record in this case, 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 against the taxpayer including all jurisdictional elements was established by the admission into evidence of Notices of Tax Liability number 00 00000000000000 through 00 00000000000000 showing tax due, including penalties, of \$596,451.92 for the audit period December 1998 through March 2005. Department Exhibit ("Ex.") 1.
2. The taxpayer, a business registered as a subchapter S corporation with the federal Internal Revenue Service, located in Anywhere, Illinois, is engaged in the retail sale of used automobiles and other used vehicles. Transcript of hearing proceedings October 15, 2008 ("Tr.") p. 6; Department Exhibit ("Ex.") 1. The taxpayer is owned and operated by John Doe and Jim Doe. Department Ex. 1.
3. The taxpayer is registered to file and files ST-556 sales tax returns reporting tax due on retail sales of motor vehicles. *Id.*
4. In March 2005, the taxpayer was the subject of a criminal investigation by agents of the Federal Bureau of Investigation ("FBI") which covered the audit period noted above. *Id.* At the commencement of its investigation, the FBI seized all of the taxpayer's books and records and its entire inventory of unsold vehicles. *Id.*

5. During its investigation, special agents of the FBI obtained and reviewed records pertaining to all of the taxpayer's sales during the aforementioned period including deal jackets, sales invoices, copies of ST-556 sales tax returns and copies of vehicle title applications. Tr. p. 44; Department Ex. 1.
6. In the course of its investigation, the FBI determined that the taxpayer obtained new titles for some of the vehicles it sold during the audit period from the Secretary of State's office without filing ST-556 sales tax returns or paying sales taxes to the Department. Tr. pp. 6, 13, 30-32; Department Ex. 1.
7. After completing its investigation, the FBI advised the Department's head of tax litigation that the taxpayer had failed to file ST-556 returns reporting all of its motor vehicle sales. Tr. pp. 13, 14; Department Ex. 1. The FBI also turned over to the Department a list showing 343 vehicle sales that it determined had not been reported as sales on ST-556 forms filed with the Department. Department Ex. 1, 2.<sup>1</sup>
8. The Department's tax litigation section turned over the FBI's report of its investigation of the taxpayer to the Department's audit bureau and asked the audit bureau to determine whether the taxpayer had underreported its state sales taxes. Department Ex. 1.
9. Mr. Angelo Lolis, an auditor with the Department's audit bureau, was assigned to audit the taxpayer for the aforementioned tax period during the summer of 2005. Tr. pp. 11-13; Department Ex. 1, 2. During the course of this audit Mr. Lolis examined the FBI's summary of its findings pursuant to its investigation of the taxpayer's books

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<sup>1</sup> The record does not indicate whether anyone was criminally charged or convicted as a result of the FBI's investigation of the taxpayer.

and records including a list of 343 ST-556 returns that were prepared but not filed with the Department. Department Ex. 1. During this audit, the Department's auditor did not personally review any of the books and records relied upon by the FBI as a basis for the conclusions indicated in the FBI's list of untaxed sales the auditor reviewed. Tr. pp. 14-24; Department Ex. 1. These records were confiscated by the FBI when it commenced its investigation of the taxpayer and were not made available to the Department by the FBI. Tr. p. 44; Department Ex. 1.<sup>2</sup> As a result of this investigation, Mr. Lolis found that the taxpayer had underreported its taxable sales by \$3,855,207.23 during the audit period in controversy and that it had over-reported the amount of trade-in vehicles received during this period. Tr. pp. 32-39, 53; Department Ex. 1, 3-5.

**10.** Mr. Lolis determined the taxpayer's Retailers' Occupation Tax liability for underreported sales by comparing vehicle sales shown on ST-556 returns the taxpayer filed with the Department to vehicle sales shown on the FBI's list of unreported sales for which ST-556 returns were prepared but not filed. Tr. p. 14; Department Ex. 1. He adjusted the taxable amount due as shown on the FBI list of unreported and untaxed sales to account for non-taxable taxes and license fees. Tr. pp. 33, 34; Department Ex. 1, 3. To determine the portion of this tax base to which the City of Anywhere tax rate and the suburban tax rate applied, the auditor determined the percentage of total sales that were to Anywhere residents and the percentage of sales that were made to non-Anywhere residents based on the taxpayer's filing history. Tr.

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<sup>2</sup> The record does not indicate whether these records were ever requested by the taxpayer or its counsel.

pp. 34, 35; Department Ex. 1, 3, 4. He arrived at a liability amount by applying the applicable state and local tax rate to the amounts determined in the manner described above. Department Ex. 3. Using this methodology, he determined that the total amount of tax due on the taxpayer's unreported and untaxed vehicle sales was \$306,103.45. *Id.*

**11.** Mr. Lolis determined the amount of disallowed trade-ins by comparing the percentage of vehicle sales reported as trade-ins on ST-556 forms with the percentage of vehicle sales determined to be trade-ins by the FBI on vehicle sales that the FBI determined had not been reported to the Department. Tr. pp. 36-39; Department Ex. 5. Using this methodology, he determined the total amount of disallowed trade-ins. *Id.* Upon applying the City of Anywhere and suburban tax rates to the portion of disallowed trade-ins attributed to these locations, the auditor determined that the tax due as a result of the disallowed trade-ins was \$158,124. Department Ex. 5.

**12.** Prior to and during the hearing in this case, the taxpayer did not produce any Z tapes, register tapes, daily sales reports or any other source documentation to substantiate the number of sales it completed during the tax period in controversy.

**Conclusions of Law:**

The Retailers' Occupation Tax Act ("ROTA") imposes a tax upon persons engaged in the business of selling at retail tangible personal property. 35 ILCS 120/2.

Section 7 of the ROTA provides in part as follows:

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 of the specific trade and other pertinent papers and documents. ... All books and records and other papers and documents which are required by this Act to be kept shall be kept in the English language and shall, at all times during business hours of the day, be subject to inspection by the Department or its duly authorized agents and employees. 35 ILCS 120/7.

Section 4 of the ROTA provides that the corrected return issued by the Department is *prima facie* correct and is *prima facie* evidence of the correctness of the amount of tax due, as shown therein. 35 ILCS 120/4. The burden shifts to the taxpayer to overcome this presumption of validity once the Department establishes its *prima facie* case by submitting the certified copy of the corrected return into evidence. A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826, 832 (1<sup>st</sup> Dist. 1988); Clark Oil & Refining Corp. v. Johnson, 154 Ill. App. 3d 773, 783 (1<sup>st</sup> Dist. 1987). To prove its case, a taxpayer must present more than its testimony denying the Department's assessment. Mel-Park Drugs, Inc. v. Department of Revenue, 218 Ill. App. 3d 203, 217 (1<sup>st</sup> Dist. 1991); Sprague v. Johnson, 195 Ill. App. 3d 798, 804 (4<sup>th</sup> Dist. 1990). The taxpayer must present sufficient documentary evidence to support its claim. *Id.* "Simply questioning the Department of Revenue's return or denying its accuracy does not shift the burden to the Department of Revenue." Quincy Trading Post, Inc. v. Department of Revenue, 12 Ill. App. 3d 725, 730-31 (4<sup>th</sup> Dist. 1973).

A review of the record in this case supports a finding that the taxpayer has failed to present sufficient evidence to overcome the Department's *prima facie* case. There is no evidence that the taxpayer kept adequate books and records of its sales as required by section 7 of the ROTA. Without books and records, the Department was required to

make its determination according to its best judgment and information. 35 ILCS 120/4; Puelo v. Department of Revenue, 117 Ill. App. 3d 260 (4<sup>th</sup> Dist. 1983).

In arriving at its determination, the Department primarily relied upon a summary of an investigation of the taxpayer conducted by the FBI. Department Ex. 1. Specifically, the Department's principle evidence was a list prepared by FBI agents purporting to show 343 sales made by the taxpayer that were not reported to the Department. *Id.* The Department compared the sales shown on the FBI list to sales for which returns were filed and sales tax reported and paid by the taxpayer during the audit period at issue and concluded that the taxpayer failed to report sales tax due and owing on the sales the FBI identified in its list. Tr. p. 14; Department Ex. 1. The Department also relied upon information from the FBI regarding the percentage of the taxpayer's total sales that were trade-ins. Tr. pp. 36-39. It compared the percentage of trade-in sales the FBI indicated in its investigation findings with the percentage of trade-ins shown on the taxpayer's returns that were filed for the tax period in controversy to arrive at its conclusion that trade-ins shown on the taxpayer's returns as filed were overstated. *Id.* The Department did not review or even see the books and records the FBI utilized in arriving at its conclusions. Department Ex. 1.

The taxpayer contends that the information relied upon by the Department is hearsay and therefore is insufficient to show that the sales determined by the FBI giving rise to the Department's assessment were actually made. Specifically, the taxpayer argues as follows:

This audit was based on information provided by the FBI. That's without question. But none of this information was substantiated by the Illinois Department of Revenue. No proof –

there's no proof – there will be no proof that these cars were ever purchased and titled and connected to the names as listed in the ST-556s provided by the FBI.

I believe the audit is based upon hearsay and allegations provided by the FBI ... [.]  
Tr. p. 8.

Hearsay consists of out of court statements made by an out of court declarant offered for the truth of the matter asserted. People v. Carpenter, 28 Ill. 2d 116 (1963). The purpose of the rule excluding hearsay evidence is to exclude evidence that cannot be subject to cross-examination. *Id.* Accordingly the principle objective of the rule is to exclude evidence where the author of the statement or writing is not available to be cross-examined or questioned concerning the truth or accuracy of what was said or written. People v. Amos, 112 Ill. App. 2d 330 (2d Dist. 1969).

Reliance on hearsay is not totally impermissible in proceedings before the Department. Although reliance upon hearsay is prohibited where credible documentary evidence is presented by the taxpayer (Novicki v. Department of Finance, 373 Ill. 342 (1940)), results of audits based partly upon hearsay have been deemed worthy of consideration when the taxpayer's records are inadequate or when, as here, the taxpayer has presented no books or records. Vitale v. Department of Revenue, 118 Ill. App. 3d 210 (3<sup>rd</sup> Dist. 1983); Illini Motor Co. v. Department of Revenue, 139 Ill. App. 3d 411 (4<sup>th</sup> Dist. 1985); Puelo, *supra* at 267 (“The true rule, then, appears to be that if the taxpayer produces records from which an audit can be made, the Department may not use hearsay evidence in an effort to shore up its case; if the taxpayer produces no records, the Department may use its best judgment and information, including what would otherwise be objectionable as hearsay, in producing its corrected return.”).

Again, as the administrative law judge reminded the taxpayer's counsel repeatedly during the hearing in this matter, it is the taxpayer's burden to overcome the Department's *prima facie* case. A.R. Barnes, supra; Clark Oil & Refining, supra. Department regulations allow this taxpayer to have requested, at least, the documents the Department relied upon in making its determination, and any documents used by the FBI in arriving at its findings even though the FBI confiscated all of the taxpayer's records when it commenced its investigation. 86 Ill. Admin. Code, ch. I, section 200.125. Certainly, the taxpayer has indicated no reason why it could not have obtained its books and records from the FBI and, if exculpatory, used them to rebut the Department's *prima facie* case. It has completely failed to do so and, as a consequence, has failed to meet its statutory burden to rebut the presumed correctness of the Department's findings in order to prevail.

Accordingly, I find that the Department's *prima facie* case was established when certified copies of the Notices of Tax Liability at issue were admitted into evidence. In response, the taxpayer has failed to present any evidence identified with its books and records showing that the Department's determination was incorrect or inaccurate. I recommend, therefore, that the Director finalize Notices of Tax Liability number 00 00000000000000 through 00 00000000000000 as issued, with interest to accrue pursuant to statute.

Ted Sherrod  
Administrative Law Judge

Date: January 8, 2009