

STATE OF NEW YORK  
TAX APPEALS TRIBUNAL

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In the Matter of the Petition :  
of :  
**ATLANTIC HOUSE YEMEN RESTAURANT, INC.** : DECISION  
for Revision of a Determination or for Refund :  
of Sales and Use Taxes under Articles 28 and 29 :  
of the Tax Law for the Period December 1, 1983 :  
through November 30, 1985 :

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Petitioner Atlantic House Yemen Restaurant, Inc., 144 Atlantic Avenue, Brooklyn, New York 11201, filed an exception to the determination of the Administrative Law Judge issued on December 28, 1989 with respect to its petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1983 through November 30, 1985 (File No. 803700). Petitioner appeared by John A. Pannone, Esq. The Division of Taxation appeared by William F. Collins, Esq. (C. Roger Jenkins, Esq., of counsel).

Petitioner filed a brief on exception. The Division of Taxation filed a letter in lieu of a brief.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

***ISSUE***

Whether the Division of Taxation properly resorted to external indices in calculating and assessing additional tax liability against petitioner.

***FINDINGS OF FACT***

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

During the period in question petitioner, Atlantic House Yemen Restaurant, Inc., operated an Arabic-style restaurant located at 144 Atlantic Avenue in Brooklyn, New York.

On January 30, 1986, the Division of Taxation issued a letter to Atlantic House Yemen Restaurant, Inc. indicating that petitioner's sales tax returns for the period March 1, 1983 through November 19, 1985 would be subjected to a field audit. This letter advised petitioner that all books and records pertaining to its sales tax liability for said period should be available for review. The letter specified such records to include journals, ledgers, sales invoices, purchase invoices, cash register tapes, exemption certificates and all other sales tax records. Attached to this letter was a second page consisting of a checklist specifying records required for audit.

At the time of the audit appointment petitioner, by its accountant, was able to provide payroll records for the period January 2, 1984 through November 19, 1985, but no other records of the business. In the absence of any records other than payroll records, the auditor concluded that petitioner's records were inadequate for the purpose of conducting a detailed audit and, hence, determined to use external indices in an effort to estimate petitioner's sales and its sales tax liability.

The auditor utilized petitioner's payroll records, and the amount shown thereon of \$34,585.00, in comparison to a Dun and Bradstreet Cost of Doing Business Survey pertaining to the restaurant industry. More specifically, the Dun and Bradstreet report utilized indicated that payroll constituted 15.52% of gross sales. Therefore, the auditor divided the payroll amount (\$34,585.00) by such 15.52% payroll factor to calculate estimated gross sales of \$222,841.00. Said amount was reduced by the amount of sales reported by petitioner per sales tax returns, resulting in unreported taxable sales of \$167,506.00. The auditor applied the tax rate then in effect against total adjusted taxable sales, calculating tax due in the amount of \$18,384.38. Reduction thereafter by the amount of tax paid per returns (\$4,564.64), resulted in an unpaid sales tax liability of \$13,819.93.

In addition to the foregoing, the auditor obtained information relative to the November 19, 1985 sale of the subject business. More specifically, the auditor determined that the selling price of the business (per a bulk sale notification received by the Division of Taxation) included the sale of fixed assets valued at \$25,000.00. The auditor was unable to confirm that sales tax had been paid on any of such fixed assets at the time of their acquisition, and thus imposed tax of \$2,062.50 thereon, based on the stated \$25,000.00 value of such assets.

On February 20, 1986, the Division of Taxation issued to petitioner, Atlantic House Yemen Restaurant, Inc., a Notice of Determination and Demand for Payment of Sales and Use Taxes Due assessing tax due in the amount of \$15,882.43, plus penalty (Tax Law § 1145[a][1]) and interest. This notice was premised upon the results of the field audit of petitioner as described above.

No documentary evidence, including source documents or otherwise, was offered by petitioner at hearing. Petitioner's accountant offered testimony as to his opinion that the sales tax returns filed by petitioner were accurate. He testified that said returns were prepared based on "slips of paper" reflecting petitioner's monthly sales as given to petitioner's accountant by its sole owner and operator, one Alawi Almontaser. Petitioner's accountant testified, based on his visits to the restaurant both to perform accounting services and to dine, that the restaurant "rarely did much business or made money." He testified that the restaurant was operated essentially on a "give away" basis and was kept open "only for the purpose of ultimately selling and/or renting the premises." On the basis of such testimony, petitioner takes the position that the Dun and Bradstreet payroll factor utilized by the auditor was unrealistic and inappropriate for application to this taxpayer given its method of operation.

### ***OPINION***

In the determination below the Administrative Law Judge found that petitioner supplied none of the records legitimately requested by the Division of Taxation (hereinafter the "Division") for purposes of conducting an audit. Since petitioner provided no evidence at hearing that its records were at any time maintained or available in a complete, adequate or

accurate fashion, and in fact gave indications to the contrary, the Administrative Law Judge held that the auditor was clearly justified in resorting to external indices in arriving at a determination of petitioner's tax liability. The Administrative Law Judge further held that petitioner's general assertions that the sales tax returns were accurate as filed, and that the index used was not appropriate were both unpersuasive and unsupported on the facts of this case. Lastly, the Administrative Law Judge held that petitioner advanced no facts upon which to conclude that there existed reasonable cause for the abatement of penalty.

On exception, petitioner alleges the auditor's conclusion that petitioner's records were inadequate for the purpose of conducting a detailed audit was arbitrary and capricious. Finally, petitioner alleges that a copy of the external index utilized by the Division was not introduced into the record and the index is, therefore, rank hearsay, the Division had no basis in fact to support its assessment as the index is not a proper "Test Period Audit" and is not the type of external indices contemplated by the statute.

In response, the Division argues that the first paragraph of the exception regarding the records produced by petitioner at audit is contrary to the facts in the record. Also, the Division notes that the statement in the Notice of Exception, "that although the records kept by petitioner were of a minimal amount he should not be penalized for his lack of keeping extensive records," is ludicrous in view of the Court of Appeals decision in Matter of Continental Arms Corp. v. State Tax Commn. (72 NY2d 976, 534 NYS2d 362) which states that those required to collect sales tax must maintain records and make them available for examination.

We affirm the determination of the Administrative Law Judge.

Where, as here, the records of the taxpayer are insufficient or inadequate to permit an exact computation of the sales and use tax due, the Division is authorized to estimate the tax liability on the basis of external indices (Tax Law § 1138[a][1]; see, Matter of Ristorante Puglia Ltd. v. Chu, 102 AD2d 348, 478 NYS2d 91, 93; Matter of Surface Line Operators Fraternal Org. v. Tully, 85 AD2d 858, 446 NYS2d 451, 452). The methodology selected must be reasonably calculated to reflect the taxes due (Matter of Ristorante Puglia Ltd. v. Chu, *supra*;

Matter of W.T. Grant Co. v. Joseph, 2 NY2d 196, 159 NYS2d 150, 157, cert denied 355 US 869, 2 L Ed 2d 75) but exactness in the outcome of the audit method is not required (Matter of Markowitz v. State Tax Commn., 54 AD2d 1023, 388 NYS2d 176, 177, affd 44 NY2d 684, 405 NYS2d 454; Matter of Lefkowitz, Tax Appeals Tribunal, May 30, 1990). While it is true that "considerable latitude is given an auditor's method of estimating sales under such circumstances as exist" in each case (Matter of Grecian Sq. v. New York State Tax Commn., 119 AD2d 948, 501 NYS2d 219, 221), certain limitations have been placed on this principle. It is necessary that the record contain sufficient evidence to allow the trier of fact to determine whether the audit has a rational basis (Matter of Grecian Sq. v. New York State Tax Commn., supra). Further, we have held that the record must contain information identifying the external index used by the Division to establish a rational basis for the audit methodology employed (Matter of Fokos Lounge, Tax Appeals Tribunal, March 7, 1991; see also, Matter of Fashana, Tax Appeals Tribunal, September 21, 1989). Such information is necessary in order to provide petitioners with an opportunity to meet their burden of proving such methodology unreasonable (Matter of Basileo, Tax Appeals Tribunal, May 9, 1991). The burden then rests with the taxpayer to show by clear and convincing evidence that the methodology was unreasonable or that the amount assessed was erroneous (Matter of Meskouris Bros. v. Chu, 139 AD2d 813, 526 NYS2d 679; Matter of Surface Line Operators Fraternal Org. v. Tully, supra).

The record is clear in this case that the resort to an external index was proper since petitioner's records were clearly insufficient and inadequate. The Division's auditor testified that the only records supplied by petitioner were, "The payroll, he provided payroll for two years, 1984 and 1985" (Tr., p. 13, lines 14, 15). In fact, petitioner's accountant, when asked "Did you keep books and records for this restaurant?" (Tr., p. 23, lines 20, 21), testified "I copied the information that he had on slips of paper for every month for every quarter of his total sales, and this is how I determined the total sales and the total taxable sales were reflected in the sales tax forms" (Tr., pp. 23, 24). Petitioner's accountant also testified that he did not audit the records submitted to him by management (Tr., p. 24). The auditor, therefore, was

justified in his use of external indices to calculate the taxes due. The issue before us is whether the external index chosen by the Division is supported by a rational basis.

In this case, the Division utilized an industry index for eating places from a Dun and Bradstreet Cost of Doing Business Survey which listed under the heading of Selected Operating Expenses, a column for salaries and wages with a percentage factor of 15.62%. The information compiled on this chart is derived from representative samples of the total of all Federal income tax returns filed for the 1969 year by proprietorships and partnerships (see Exhibit F). Contrary to the assertion of petitioner, a copy of this Survey was introduced into the record at the hearing (see Exhibit F). In any event, hearsay evidence is admissible in an administrative hearing (Matter of Meskouris Bros. v. Chu, supra).

Further, while petitioner's representative at hearing questioned the Division's use of the Survey on the basis that it covered all kinds of restaurants and was not limited to the particular type of restaurant that was operated by this particular corporation, petitioner failed to establish at the hearing that the basis for this audit as specifically applied to its restaurant business was unreasonable. Where the taxpayer's records thwart an accurate reckoning, the Division is not required to compute tax with a high degree of precision (Matter of Meskouris Bros. v. Chu, supra). Petitioner failed to submit any credible evidence or supporting documentation to prove, as alleged, that the audit methodology was unreasonable or the assessment was erroneous; therefore, we sustain the audit and assessment made by the Division.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of petitioner Atlantic House Yemen Restaurant, Inc. is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Atlantic House Yemen Restaurant, Inc. is denied; and

4. The Notice of Determination and Demand for Payment of Sales and Use Taxes Due, dated February 20, 1986, is sustained.

DATED: Troy, New York  
July 11, 1991

/s/John P. Dugan  
John P. Dugan  
President

/s/Francis R. Koenig  
Francis R. Koenig  
Commissioner

/s/Maria T. Jones  
Maria T. Jones  
Commissioner