STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
FRANK AURIEMMA	:	DECISION DTA No. 806542
for Revision of Determinations or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period September 1, 1983 through November 30, 1986.	:	

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on August 1, 1991 with respect to the petition of Frank Auriemma, 21 Jacob Road, Plainview, New York 11803 for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1983 through November 30, 1986. Petitioner appeared by Swartz & Swartz, Esqs. (Ronald J. Swartz, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Vera R. Johnson, Esq., of counsel).

The Division of Taxation filed a brief on exception. Petitioner filed a brief in response. The Division of Taxation's request for oral argument was denied.

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

ISSUES

I. Whether the Division of Taxation's audit provided a rational basis for determining additional sales tax due.

II. Whether, if the audit provided a rational basis for determining additional sales tax due, petitioner has established that certain adjustments to the audit should nonetheless be made to better reflect his sales tax liability for the period at issue.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "12(6)" which has been modified. The Administrative Law Judge's findings of fact and the modified finding of fact are set forth below.

Petitioner, Frank Auriemma, during the period at issue owned and operated two Carvel ice cream stores in New York City: one in Richmond Hill, Queens (hereinafter "Richmond store"); the other on Nostrand Avenue in Brooklyn (hereinafter "Brooklyn store"). Petitioner has owned and operated Carvel ice cream stores for 39 years. The Richmond and Brooklyn stores were financially successful operations with total gross sales reported by petitioner during the audit period (of 3 years and 3 months) of $733,706.09 and $565,599.91, respectively. Of the total gross sales from his two stores of $1,299,306.00, petitioner remitted sales tax on reported total taxable sales for the two stores of $296,296.00. Therefore, petitioner reported approximately 23% of his total gross sales as subject to sales tax.

The Division of Taxation issued two notices of determination and demands for payment of sales and use taxes due dated August 21, 1987 against petitioner asserting (i) tax due of $30,658.32, plus penalty and interest, and (ii) penalty (under Tax Law § 1145) of $1,204.42. The notice which asserted tax due included the following explanation:

> "The following taxes have been determined to be due in accordance with Section 1138 of the Tax Law, and are based on an audit of your records."

This notice also advised petitioner that:

> "The tax assessed herein has been estimated or determined to be due in accordance with the provisions of section 1138 of the Tax Law...."

Evelyn Sandler, the sales tax auditor responsible for the audit of petitioner's records, testified at the hearing herein that she determined on audit that petitioner's taxable percentage of gross sales was (i) 65.52% for sales tax quarters ending May 31st and August 31st, so-called "summer season" quarters, and (ii) one-half of such percentage, or 32.76%, for sales tax quarters ending November 30th and February 28th, so-called "winter rate" quarters. The auditor

accepted the amounts reported by petitioner as his gross sales and calculated taxes asserted as due by applying these percentages to petitioner's gross sales as reported for each of the 13 sales tax quarters at issue herein. For example, the auditor determined additional taxable sales for the first sales tax quarter at issue herein (the three-month period, September 1 through November 30, 1983) as follows:

Gross Sales (Reported by Petitioner) Per ST-100	Audited Taxable Rate	Adjusted Taxable Sales	Reported Taxable Sales
$98,398.00	32.76%	$32,235.00	$14,945.00

Difference	Tax Due @ 8¼%
$17,290.00	$1,426.42

In this fashion, the auditor calculated tax due of $30,658.32.

At both stores, petitioner sells soft ice cream for immediate consumption in cones and sundaes, and pre-packaged products for off-premises consumption, such as ice cream cakes, frozen cones and reduced calorie products. Consequently, all of petitioner's gross sales did not constitute taxable sales, and, as a result, the heart of the audit was the auditor's estimate of the percentage of petitioner's gross sales subject to sales tax.

The auditor determined the taxable percentage of gross sales for the summer season quarters by analyzing petitioner's purchases of items (such as cones, cups and other types of containers) that were used with ice cream to make products that when sold would constitute taxable sales. According to the auditor, petitioner did not have all of his "purchase bills" for the entire audit period, and, as a result, she performed a "purchase test" for the sales tax quarter June 1 through August 31, 1985. The results of such test period were then projected over the entire audit period after an adjustment for "winter rate" quarters.

More specifically, the auditor estimated taxable sales of $90,955.00 for the three-month test period as follows:

Item #	Description	# of Packages	# in Package	Total	Selling Price	Gross Sales	% of Taxable Use	Taxable Sales
707	sundae cup	12	1,000	12,000	$1.95	$23,400	50%	$11,700
723	cup for thick shake	17	1,000	17,000	1.95	33,150	50%	16,575
1000	small cone	26	1,000	26,000	.90	23,400	100%	23,400
1002	large cone	6	600	3,600	.90	3,240	50%	1,620
1006	sugar cone	15	800	12,000	.90	10,800	100%	10,800
713	plastic quart	5	500	2,500	3.00	7,500	0%	0
712	plastic pint	10	500	5,000	1.95	9,750	0%	0
630	banana barge	2	500	1,000	1.95	1,950	100%	1,950
633	small dish	1	3,000	3,000	.90	2,700	100%	2,700
705	½ pint container	9	1,200	10,800	1.95	21,060	100%	21,060
777	cups for egg cream	1	1,000	1,000	1.15	1,150	100%	1,150
								$90,955

She then determined that the percentage of taxable use for this test quarter was 65.52% ($90,955.00 divided by $138,819.00, gross sales reported by petitioner for the quarter). As noted above, this percentage was then applied to all sales tax quarters during the audit period which ended on May 31st and August 31st. The auditor testified that the percentage of taxable use would be less in colder periods than warmer periods:

> "[T]aking into consideration there are winter months, we reduced -- we used half and half, 65.52 for the warm months and 32.76 for the colder months...."

Consequently, for all sales tax quarters during the audit period which ended on November 30th and the last day of February, the auditor applied the smaller percentage of 32.76% to petitioner's reported gross sales to determine taxable sales for such quarters.

The auditor, by utilizing the audit methodology detailed above, determined "adjusted taxable sales" for the audit period of $667,912.00, a difference of $371,616.00 from petitioner's reported taxable sales of $296,296.00. As noted above, petitioner reported 23% of his total sales as taxable sales while the auditor's position was that 51% of petitioner's total gross sales during the audit period were subject to sales tax.

At the hearing commenced on August 2, 1990, petitioner introduced into evidence as Exhibit "4" schedules, which recalculated tax due, based upon an analysis of petitioner's purchases of the 11 items detailed above, for each month during 1985, not just the three-month

period June 1 through August 31, 1985. In addition, the purchases were broken down between the Richmond store and the Brooklyn store. Taxable percentages of gross sales were calculated by petitioner for each of the four sales tax quarters ending in 1985, for each store individually, as follows:

	Taxable Sales	Gross Sales	Taxable Percentage
(Richmond Store)			
January 1985	$ 1,796.00		
February 1985	10,030.70	$ 64,803.00	25.03%[1]
March 1985	13,544.20		
April 1985	12,233.90		
May 1985	16,335.10	105,678.00	39.85%
June 1985	16,240.60		
July 1985	10,636.00		
August 1985	10,894.20	138,819.00	27.21%
September 1985	6,814.40		
October 1985	8,950.30		
November 1985	4,515.00	85,715.00	23.66%
December 1985	4,396.60		
Total	$116,387.00	$395,015.00	29.46%
(Brooklyn Store)			
January 1985	$ 0.00		
February 1985	4,002.40	$ 64,803.00	6.18%[2]
March 1985	8,454.20		
April 1985	6,162.30		
May 1985	10,701.90	105,678.00	23.96%
June 1985	13,518.50		
July 1985	13,752.70		
August 1985	13,144.80	138,819.00	29.11%
September 1985	8,530.40		
October 1985	5,520.60		
November 1985	5,932.70	85,715.00	23.31%
December 1985	0.00		
Total	$ 89,720.50	$395,015.00	22.71%

[1] Petitioner apparently added his estimated taxable sales of $4,396.60 for December 1985 to those for January and February to determine the percentage of gross sales that were taxable for the quarter ending February 28, 1985.

[2] In a fashion similar to that described in Footnote "1," petitioner apparently added his estimated taxable sales for December 1985 of zero to those for January and February to determine the percentage of gross sales that were taxable for the quarter ending February 28, 1985.

In calculating taxable sales for each month of 1985 as shown above, petitioner used lower selling prices for his products than the auditor. He also used reduced percentages of taxable use[3] for the following items:

Item	% of Taxable Use Auditor	Petitioner's Exhibit "4"
small cone	100%	93%
large cone	50%	93%
sugar cone	100%	95%
small dish	100%	70%
½ pint container	100%	70%
cups for egg creams	100%	40%

As an example, petitioner calculated his taxable sales in his Richmond store for the month of June 1985 of $16,240.60 as follows:

Item #	Description	# of Packages	# in Package	Total	Selling Price	Gross Sales	% of Taxable Use	Taxable Sales
707	sundae cup	4	1,000	4,000	$1.66	$6,640	50%	$ 3,320.00
723	cup for thick shake	2	1,000	2,000	1.66	3,320	50%	1,660.00
1000	small cone	5	1,000	5,000	.74	3,700	7%	3,441.00
1002	large cone	0	600	0	1.15	0	7%	0
1006	sugar cone	4	800	3,200	.79	2,528	5%	2,401.60
713	plastic quart	1	500	500	3.00	1,500	100%	0
712	plastic pint	2	500	1,000	1.95	1,950	100%	0
630	banana barge	0	250	0	3.23	0	0%	0
633	small dish	1	3,000	3,000	.74	2,220	30%	1,554.00
705	½ pint container	4	1,200	4,800	1.15	5,520	30%	3,864.00
777	cups for egg cream	0	1,000	0	.74	0	60%	0
								$16,240.60

Prior to the continuation of the hearing in this matter on October 23, 1990, an auditor, Irving Silverstein, reviewed petitioner's alternate calculation of tax due and discovered a major flaw in petitioner's calculation. In calculating the taxable percentages of 29.46% for the

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[3] Petitioner, on his Exhibit "4," showed so-called "discounts" instead of percentages of taxable use. For example, he showed a 7% discount for small cones, which has been converted into a percentage of taxable use of 93%. Other discounts have been similarly converted into percentages of taxable use.

Richmond store and 22.71% for the Brooklyn store, as detailed above, petitioner used total gross sales for both stores as the denominator in each calculation, rather than only total gross sales for the particular store as compared to taxable sales for the particular store.

Mr. Silverstein pointed out that if taxable sales of $116,387.00 for the Richmond store were added to taxable sales of $89,720.50 for the Brooklyn store, petitioner had estimated, in his Exhibit "4," total taxable sales for his two stores for 1985 of $206,107.50, which represented 52% of petitioner's gross sales for 1985 of $395,015.00. Mr. Silverstein opined that such percentage lent support to Ms. Sandler's calculation of tax due since she had estimated that petitioner's taxable sales for the audit period were $667,912.00 out of gross sales of $1,299,306.00, or 51.4% of gross sales.

Mr. Silverstein advised petitioner of his error, and at the continuation of the hearing in this matter on October 23, 1990, petitioner introduced into evidence as Exhibit "5" a revised Exhibit "4," which showed substantially reduced percentages of taxable use as follows:

Item	Auditor	Petitioner's Exhibit "4"	Petitioner's Exhibit "5"
small cone	100%	93%	50%
large cone	50%	93%	50%
sugar cone	100%	95%	5%[4]
small dish	100%	70%	30%
½ pint container	100%	70%	5%
cups for egg creams	100%	40%	40%

Utilizing these reduced percentages of taxable use, petitioner (as he did in his Exhibit "4") recalculated tax due, based upon an analysis of petitioner's purchases of the 11 items detailed above, for each month during 1985, and he once again allocated the purchases between the Richmond store and the Brooklyn store. However, taxable sales for the Richmond and

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[4] Petitioner, on his Exhibit "5," showed so-called "discounts" instead of percentages of taxable use as he had done on his Exhibit "4." These discounts have been restated as percentages of taxable use.

Brooklyn stores were then added together. Taxable percentages of gross sales were recalculated by petitioner for each of the four sales tax quarters ending in 1985 as follows:[5]

	Richmond Taxable Sales	Brooklyn Taxable Sales	Total Taxable Sales	Gross Sales	Taxable Percentage
January 1985	$ 899.00	$ 0.00	$ 899.00		
February 1985	5,977.40	2,469.00	8,446.40	$ 64,803.00	17.10%[6]
March 1985	7,866.30	5,746.10	13,612.40		
April 1985	6,242.50	4,014.00	10,256.50		
May 1985	9,228.10	7,688.10	16,916.20	105,678.00	38.59%
June 1985	7,898.40	9,504.00	17,402.40		
July 1985	5,862.80	8,713.30	14,576.10		
August 1985	5,888.40	8,643.70	14,532.10	138,819.00	33.50%
September 1985	3,266.40	5,516.60	8,783.00		
October 1985	4,233.70	3,153.20	7,386.90		
November 1985	2,162.20	3,215.60	5,377.80	85,715.00	25.14%
December 1985	1,733.60	0	1,733.60		
Total	$61,258.80	$58,663.60			

Petitioner then applied the above taxable percentages to other quarters during the audit period ending in the same month and calculated tax due of $7,635.07 as follows:

	Gross Sales	Taxable Percentage	Taxable Sales
November 1983	$ 98,398.00	25.14%	$ 24,736.05
February 1984	74,487.00	17.10%	12,734.62
May 1984	91,060.00	38.59%	35,143.47
August 1984	135,885.00	33.50%	45,527.58
November 1984	93,562.00	25.14%	23,520.34
February 1985	64,803.00	17.10%	11,079.00
May 1985	105,678.00	38.59%	40,785.10
August 1985	138,819.00	33.50%	46,510.60
November 1985	85,715.00	25.14%	21,547.70
February 1986	56,235.00	17.10%	9,614.18
May 1986	119,090.00	38.59%	45,961.29
August 1986	148,964.00	33.50%	49,909.63
November 1986	86,610.00	25.14%	21,772.69
		Total	$388,842.25

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[5] Petitioner did not calculate separate taxable percentages of gross sales for each store in Exhibit "5" (as he had done in his Exhibit "4").

[6] In a fashion similar to that described in Footnotes "1" and "2," petitioner apparently added his estimated taxable sales for December 1985 of $1,733.60 to that for January and February to determine the percentage of gross sales that were taxable for the quarter ending February 28, 1985.

Reported	296,296.00
Deficiency	$ 92,546.25
Tax (.0825)	($ 7,635.07)

The auditor used selling prices for each of the 11 items noted above, substantially higher than the selling prices used by petitioner in his alternate estimate of his taxable sales for the period at issue. The auditor testified that she went to one of the stores on August 28, 1986 and "took the prices off the board". At first, she testified on cross-examination that she did not know if the selling prices were "net of sales tax or...[included] sales tax". However, later in her cross-examination, the auditor testified that the posted prices "did not indicate that tax was included." The auditor visited only one of the two stores in the course of her audit.

In contrast, petitioner introduced into evidence photocopies of price reports prepared by Carvel which were included in inspection reports by Carvel representatives. These reports show the following selling prices at issue:

Richmond Store - Report Dated December 20, 1985

sundae[7] cup	thick shake	small cone	large cone	sugar cone	banana barge	small dish	large[8] dish	½ pint	drinks small	drinks large
$1.95	$2.35	$.90	$1.35	--	$3.75	$.90	$1.35	--	$.60	$ .90

Brooklyn Store - Reported Dated July 24, 1986

$1.95	$2.60	$.90	$1.35	illegible	$3.95	$.90	$1.35	--	$.70	$1.15

Richmond Store - Report Dated June 24, 1984

$1.80	$2.20	$.80	$1.25	--	$3.50	$.80	$1.25	--	$.60	--

[7] Three of the four inspection reports show more than one price for sundaes. The lowest price is shown in the schedule above.

[8] Three of the four inspection reports do not show prices for half pint containers, but they all show prices for large dishes which are included in the schedule above. It is unexplained why the auditor's listing does not include a price for a large dish of ice cream, since it appears that this was an item sold by petitioner subject to sales tax. Similarly, it is unexplained why the auditor's listing does not include a price for small and large drinks, which were presumably also subject to sales tax.

Brooklyn Store - Report Dated September 27, 1984

$1.80	--	$.80	$1.25	$.05	$3.50	$.80	$1.25	$1.20	$.60	$1.10

Petitioner also testified that his selling prices included sales tax:

> "In the front of the store we have a price [sic] that says 'sales tax included'."

Petitioner indicated that the selling prices shown on the Carvel inspection reports were his posted prices, which included sales tax. A close review of these inspection reports does not disclose whether or not sales tax was included in the selling prices.

The auditor used percentages of taxable use higher than petitioner in his Exhibit "4" for several items, as noted above. But, in comparison to petitioner's Exhibit "5," the percentages of taxable use used by the auditor were substantially higher than petitioner's:

% of Taxable Use[9]

Item	Auditor	Petitioner's Exhibit "4"	Petitioner's Exhibit "5"
small cone	100%	93%	50%
large cone	50%	93%	50%
sugar cone	100%	95%	5%
small dish	100%	70%	30%
½ pint container	100%	70%	5%
cups for egg creams	100%	40%	40%

In support of his lower percentages of taxable use, petitioner's only evidence was his own testimony. The following is a summary of Mr. Auriemma's testimony with regard to why his proposed percentages of taxable use (or discounts) were more accurate than the auditor's:

(1) Small cone - The auditor failed to allow for breakage and for "giveaways" to people who "buy a quart of ice cream and we give them empty cones" and to local schools and charities who apparently purchase bulk ice cream with cones provided at no charge. In his brief, petitioner argued that the auditor failed to allow for promotional offerings such as two-for-one promotions of ice cream cones. However, petitioner's testimony concerning such

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[9] Petitioner's "discounts" shown on his exhibits have been converted into percentages of taxable use.

promotions was with regard to sales of sundaes and thick shakes. As noted above, the auditor allowed a 50% discount for such items.

(2) Large cone - According to petitioner, "[e]xactly the same situation" as the small cones.

(3) Sugar cone - Petitioner does not put ice cream in a sugar cone unless it is requested, and there is an additional charge and only "[o]nce in a while people will buy sugar cones...." According to petitioner, 90% of the sugar cones are used for brown bonnets, a pre-made frozen item that is nontaxable.

(4) Small dish - Petitioner testified that he used the three-ounce cup for six or seven different pre-made take-home items that were nontaxable, including tortonis, tarts, nutty rolls and sprinkle cups.

(5) Half-pint container - According to petitioner, this container is used for "Thinny Thins," a take-home frozen item.

We modify finding of fact "12(6)" of the Administrative Law Judge's determination to read as follows:

> (6) Cups for egg creams - Petitioner testified that he and the auditor agreed that 60% of the use of the cups was nontaxable. However, earlier in his testimony, petitioner seems to assert that the auditor would not accept the 60% figure, insinuating that the auditor did not take into consideration petitioner's employees' personal use of cups."[10]

According to the auditor, petitioner did not have all of his purchase invoices:

> "He did not have the purchase invoices to match the books.... [T]he test period for purchases had missing invoices, and [the auditor wrote petitioner] asking if there were payments from the cash disbursements books showing certain items because there were no bills that could be matched up.

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[10] Finding of fact "12(6)" of the Administrative Law Judge's determination read as follows:

> "Cups for egg creams - Petitioner mistakenly testified that he and the auditor agreed on the lower percentage of taxable use. However, earlier in his testimony petitioner complained that the auditor did not take into consideration his employees' personal use of cups.

We modified finding of fact "12(6)" to more accurately reflect the record.

> "And there were two invoices in the batch that weren't in the books at all. I asked for an explanation of the discrepancies and requested he call Formula Service Division who supplies the paper items, et cetera, to Carvel stores, that he may be able to have duplicates made and have this matter straightened out."

The auditor noted that she never received purchase invoices that apparently were missing for the test period, June 1 through August 31, 1985.[11]

However, at the hearing on August 1, 1990, petitioner brought forward several hundred invoices that he claimed represented his purchase invoices for the entire year 1985 and which formed the basis for his alternative analysis of tax due described above. The revised calculation described above, was also based on such invoices.

The auditor was advised by the Administrative Law Judge to review the 200 or so invoices to "see whether there is anything new here or whether it's the same situation, that invoices are not in order or there appears to be some missing or -- whatever it might be, but since they are coming forward with a substantial amount of documentation now, between today and our reconvening they should -- the auditors should really take another look at it." At the continuation and completion of the hearing on October 23, 1990, the Division of Taxation did not offer any response concerning the completeness and accuracy of the documents brought forward on August 2, 1990.

According to petitioner, at a seminar in September 1990, he obtained a document labeled "Carvel College, Control Return Per Gallon," which included information concerning sales at Carvel Corporation's three company units in the New York City metropolitan area. This document shows the following percentage of sales:

Product Type	% of Sales
Cakes	47.60
Take-home	30.00
Fountain	20.00
Bulk	2.40
Total	100.00%

[11]The auditor testified that she "normally [does] a one-year examination of all the purchases for the store. And I could not obtain a full year of purchases."

Petitioner argues that fountain sales are subject to sales tax only, and such sales represented only 20% of total sales in the "Carvel College" analysis.

OPINION

Noting that petitioner did not challenge the Division of Taxation's (hereinafter the "Division") right to estimate his taxable sales, but rather contested the methodology used to calculate these sales, the Administrative Law Judge determined that there were certain flaws in the Division's audit methodology. Specifically, while the Administrative Law Judge upheld -- notwithstanding certain modifications described, infra -- the results of the purchase test audit conducted for the months of June through August of 1985, as well as the extension of these results to cover the quarter of March through May of 1985, he determined that the Division was not able to demonstrate that a rational basis existed for the auditor's decision to take the audit results and reduce them by 50% to account for decreased taxable sales in the winter quarters (quarters ending in February and November) of the year. Therefore, the Administrative Law Judge accepted petitioner's reported taxable sales for the winter quarters. Additionally, the Administrative Law Judge found that the auditor used incorrect selling prices in her calculations, as petitioner's posted prices already included sales tax.

On the other hand, the Administrative Law Judge determined that petitioner failed to prove by clear and convincing evidence his entitlement to further discounts based on "giveaways," cones provided free to charities, broken cones, and/or two-for-one sales of ice cream. However, the Administrative Law Judge held that petitioner had proven that "substantial reduction[s]" in the taxable use percentages of sugar cones and small dishes was in order as these items were used almost exclusively (95% and 70%, respectively) for nontaxable, pre-made take-home desserts (Determination, p. 17).

The Administrative Law Judge refused to grant a similar reduction in the taxable use of 1/2-pint containers and cups for egg creams, however, finding that these containers must necessarily be those used to hold the large dishes of ice cream and small and large drinks which petitioner

sells, as "there is no mention in the record of any other items that could be used for such sales" (Determination, p. 18).

On exception, the Division claims that both the concept of and the figure derived for the 50% "winter" reduction are rationally based. First, the Division argues that the concept of an ice cream store reducing taxable sales during the winter quarters is rationally based, in that, as the auditor testified, "common sense dictates" that ice cream stores sell more ice cream resulting in taxable sales in the summertime (Division's brief on exception, pp. 6-7, 14). Second, the Division asserts that the 50% winter reduction calculation it employed is rational, for in conducting the purchase test period audit, the auditor's review of petitioner's books and records revealed approximately 50% more purchases made by petitioner during the sales tax quarters ending in May and August (the "summer" quarters) than those ending in February and November (as noted, the "winter" quarters) (Division's brief on exception, pp. 6-8, 12, 13). Furthermore, the Division notes that petitioner's reported taxable sales for the winter quarters are 53% of petitioner's reported taxable sales for the summer quarters (Division's brief on exception, pp. 8, 9, 13). The Division argues that the auditor's uncontroverted testimony alone regarding petitioner's purchase records provides an adequate basis for reducing petitioner's summer taxable sales by 50% in the winter, and that petitioner's own records of purchases and taxable sales serve to buttress this testimony.

The Division asserts that, in any case, the rate of taxable sales it utilized for the winter quarters should be upheld because the sales in question are presumed taxable pursuant to Tax Law § 1132(c), and the fact that petitioner failed to establish any exemption from the tax enables the Division to tax 100% of the reported gross sales, although it chose to tax only 50% (Division's brief on exception, p. 14).

Finally, the Division maintains that petitioner failed to prove the assessment erroneous. Regarding the Division's alleged inflation of the sales prices due to the addition of sales tax to petitioner's posted prices, the Division contends that the only evidence of the inclusion of sales tax in the prices petitioner listed is petitioner's self-serving testimony regarding this claimed

inclusion, and that it alone is insufficient to establish by clear and convincing evidence that the Division erred by not taking this sales tax into account. Similarly, the Division asserts that it was improper for the Administrative Law Judge, based solely on petitioner's self-serving declaration, to adjust the percentage of petitioner's taxable use of sugar cones and small dishes applied by the Division in the test period audit. Petitioner's mere estimate of the percentages of taxable use to be utilized in the calculation is insufficient, claims the Division, to challenge the Division's determination of the taxes due. The Division requests that the determination be modified in light of these factors.

In response, petitioner asserts that since "purchase records and related documentation for the entire Audit Period" were made available to the auditor, sufficient to conduct a complete audit, the auditor's decision to ignore these records in favor of employing an indirect audit method was not permissible (Petitioner's reply brief, pp. 10-11). In particular, petitioner challenges the legitimacy of the Division's assumption, for purposes of conducting its purchase test, that all of the items purchased by petitioner within the test period were sold by petitioner within the same period (citing Matter of Ace Provision & Luncheonette Supply v. Chu, 135 AD2d 1070, 523 NYS2d 208; Matter of Snyder v. State Tax Commn., 114 AD2d 567, 494 NYS2d 183). The "ludicrous" outcome of the incorporation of this assumption into the Division's methodology, petitioner points out, "without allowing for double counting, improper pricing, breakage, promotional items and non-taxable uses of alleged Taxable Items, and assuming the prices that were used by the Tax Department," is that petitioner's reported gross sales for the June through August test period -- which the Division did not contest -- are nearly $5,000.00 less than petitioner's taxable sales based on purchases, as calculated by the Division -- resulting in a taxable percentage of 103.52% (Petitioner's reply brief, p. 13).

In the alternative, if the purchase test method is held to have been proper, petitioner challenges the Division's "arbitrary and capricious" decision to determine petitioner's taxable sales based only on purchases made during a three-month period -- using the three busiest months of the year, according to petitioner -- when petitioner's records for the entire year were

available (Petitioner's reply brief, p. 15). Petitioner contends that if the purchase methodology were to be employed, it would have been more accurate to apply it to the entire year's purchase records.

Finally, petitioner asks that this Tribunal uphold the various allowances granted by the Administrative Law Judge, such as that petitioner's prices as listed included sales tax, and that many of petitioner's purchases resulted in reduced taxable sales, since the Division introduced no evidence to challenge these allowances. Petitioner maintains that the Division's attempts to overturn these findings are meritless.

We affirm in all respects the determination of the Administrative Law Judge.

Tax Law § 1135(a) provides that:

> "[e]very person required to collect tax shall keep records of every sale . . . and of all amounts paid, charged or due thereon and of the tax payable thereon, in such form as the commissioner of taxation and finance may by regulation require. Such records shall include a true copy of each sales slip, invoice, receipt, statement or memorandum upon which subdivision (a) of section eleven hundred thirty-two requires that the tax be stated separately" (emphasis added).

The Division's right to resort to a test period audit to estimate taxes due by petitioner arose from the latter's failure to maintain adequate records of sales such that it would be possible for the Division to determine that tax has been charged on all taxable items (see, Matter of Licata v. Chu, 64 NY2d 873, 487 NYS2d 552; Matter of Shop Rite Wines & Liqs., Tax Appeals Tribunal, February 22, 1991). "Where the taxpayer's own failure to maintain proper records prevents exactness in determination of sales tax liability, exactness is not required" (citing Matter of Meyer v. State Tax Commn., 61 AD2d 223, 402 NYS2d 74, 78, lv denied 44 NY2d 645, 406 NYS2d 1025), and estimates by the Division regarding a taxpayer's liability are acceptable, as long as rationally based (see, Matter of Grecian Sq. v. New York State Tax Commn., 119 AD2d 948, 501 NYS2d 219; Matter of Fashana, Tax Appeals Tribunal, September 21, 1989).

Since petitioner has never asserted that he maintained adequate records of sales, it is clear that the Division had the right to use an estimate methodology. The question before us is

whether petitioner has established that the audit methodology was not reasonably calculated to reflect the taxes due (see, Matter of Ristorante Puglia, Ltd. v. Chu, 102 AD2d 348, 478 NYS2d 91).

With respect to the reasonableness of the audit, we will not address petitioner's contention that the Division should have used all of petitioner's purchase records for 1985, rather than its purchase records for only a three-month test period. Petitioner has not required us to review this issue by filing a timely exception (see, Matter of Armel, Tax Appeals Tribunal, July 23, 1992; Matter of Caleri, Tax Appeals Tribunal, August 11, 1988 [where no exception and no request for an extension to file an exception have been filed by a party within the 30-day period following the issuance of a determination, for this party to raise a new aspect of the determination in the party's reply brief would be in the nature of a cross-exception, impermissible under such circumstances according to regulation 20 NYCRR 3000.11(a)(2) of the Tribunal]; Matter of Klein's Bailey Foods, Tax Appeals Tribunal, August 4, 1988), and we see no reason to exercise our discretion pursuant to 20 NYCRR 3000.11(e)[12] to review it.

With respect to that portion of the audit methodology that has been raised for our review, petitioner has established that the audit methodology was not reasonably calculated to reflect the taxes due on sales made during the winter quarters of the audit period (quarters ending November and December of each year).

While "[c]onsiderable latitude is given an auditor's method of estimating sales" where the taxpayer's records are inadequate to prove the amount of sales (Matter of Grecian Sq. v. New York State Tax Commn., supra, 501 NYS2d 219, 221), there is a limit placed on deference to the auditor's method (see, Matter of Fashana, supra). This limit is that the record must contain sufficient evidence to allow the trier of fact to determine whether the audit had a rational basis (Matter of Grecian Sq. v. State Tax Commn., supra; Matter of Shop Rite Wines & Liqs., supra; Matter of Fashana, supra).

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[12]20 NYCRR 3000.11(e) permits the Tribunal to review the record and "to the extent necessary or desirable, exercise all the powers which it could have exercised if it had made the determination."

On the record before us, it is not clear how the auditor arrived at the 50% reduction figure for taxable sales in the winter quarters. The auditor was not able to describe the source of the 50% figure at the hearing and, in fact, gave contradictory responses to questions regarding its derivation (see, Tr., pp. 39-42). Furthermore, there is no indication in the auditor's Field Audit Report of how the auditor derived the 50% reduction figure (see, Exhibit "I"). The Report merely indicates that the taxable percentage of gross sales in the audit determination was "set as" 32.76% for the winter quarters, instead of the 65.53% summer quarters figure stemming from an analysis of the purchase records for June, July and August of 1985 (Exhibit "I").

Although the auditor testified that the "only consecutive" purchase records made available by petitioner were for June through August of 1985, and that the Division's requests for further documentation went unanswered (Tr., p. 34), this limitation did not prevent the auditor from analyzing petitioner's purchases during the months of March, April and May and determining that they were in the same relative proportion as those for the months of June through August (Tr., p. 41). For no apparent reason, the auditor did not make such an analysis for the winter quarters of the audit (Tr., p. 42). Thus, the record before us indicates neither the source of, nor any justification for, the 50% figure. Where the Division is unable to describe the bases of its audit methodology, in response to questions at the hearing, the audit methodology is irrational (see, Matter of Basileo, Tax Appeals Tribunal, May 9, 1991; Matter of Shop Rite Wines & Liqs., supra). Accordingly, we uphold the Administrative Law Judge's decision to defer to petitioner's calculation of the percentages of taxable sales for the winter quarters, as per his filed returns.

It is notable that the Division's version of the facts, set forth in its brief on exception, does not provide any insight into the source of the 50% figure. In its brief, the Division claims that it reduced petitioner's taxable sales for the winter quarters by 50% based on petitioner's purchase records (see, Division's brief on exception, pp. 2, 7). While the Division subsequently concedes that the auditor did not perform a comparative analysis to compute the exact ratio, it then attempts to justify its earlier contradictory statements by asserting that, in any case, the auditor's

conclusion "is confirmed by the Petitioner's Exhibit '5'" (Division's brief on exception, p. 7). Nevertheless, the Division then concedes that "[i]n actuality, the petitioner's purchases in the winter are 42% of the petitioner's summer purchases" (a 58% reduction)[13] (Division's brief on exception, p. 8, footnote 5).

We note that, while we agree with the Division that there is a statutory presumption pursuant to Tax Law § 1132(c) that certain types of sales are taxable[14] (see, Matter of Sol Wahba v. New York State Tax Commn., 127 AD2d 943, 512 NYS2d 542 [retail sales of electronic equipment]; Matter of Sunny Vending Co. v. State Tax Commn., 101 AD2d 666, 475 NYS2d 896 [cafeteria sales]; Matter of LaCascade, Inc. v. State Tax Commn., 91 AD2d 784, 458 NYS2d 80 [sales of vacation packages in "lump sum" rates]; Matter of Goldner v. State Tax Commn., 70 AD2d 978, 418 NYS2d 477, lv denied 48 NY2d 608, 423 NYS2d 1025 [deli sales]; Matter of Reference Lib. Guild, Tax Appeals Tribunal, August 4, 1988 [out-of-state sales]; Matter of Ellis Enters., State Tax Commn., December 20, 1983 [restaurant sales]), we reject the insinuation that this presumption satisfies the Division's burden to devise a reasonable methodology for calculating taxable sales. In short, since petitioner here has shown that, at the time of the audit, the auditor was aware that petitioner had made some amount of nontaxable sales, petitioner established that not all of its receipts during the audit period were taxable. For the Division to

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[13]Even if the record indicated that the auditor relied on an increase in purchases during the summer quarters to justify the 50% figure, this proof alone would not be sufficient to state a rational basis for the audit. While we do not dispute that a finding of increased purchases in the summer quarters would imply an increase in gross sales, such a finding would have no obvious bearing on the percentage of taxable sales -- the only issue here. The assumption of the audit, according to the Division, is that the sale of pre-packaged items is not taxable (Tr., p. 12). Yet we cannot assume, as the Division apparently urges, that increased purchases in the summer translate not into increased pre-packaged sales, but into increased taxable sales. Even the auditor acknowledged in her calculations that at least several of the items petitioner stocks are used equally for both taxable and nontaxable sales (see, Exhibit "2"), and as the Administrative Law Judge determined and we affirm, several of the items petitioner stocks are used far more for nontaxable sales than for taxable sales (see, Determination, conclusion of law "E"). Thus, increased purchases could result in increased nontaxable (pre-packaged) sales.

[14]Tax Law § 1132(c) provides, in pertinent part, that:

> "[i]t shall be presumed that all receipts for property or services of any type mentioned in subdivisions (a), (b), (c) and (d) of section eleven hundred five . . . are subject to tax until the contrary is established, and the burden of proving that any receipt . . . is not taxable hereunder shall be upon the person required to collect tax . . . ."

rely on the section 1132(c) presumption in the face of such information would be erroneous, at least in a situation where a specific certificate is not required to establish nontaxability (cf., Matter of Ace Provision & Luncheonette Supply, supra; Matter of On the Rox Liqs., Ltd. v. State Tax Commn., 124 AD2d 402, 507 NYS2d 503, lv denied 69 NY2d 603, 512 NYS2d 1026; Matter of M & B Appliance, Tax Appeals Tribunal, April 9, 1992). Rather, the obligation was on the Division here to design a reasonable audit methodology to calculate taxable versus nontaxable sales (but see, Matter of Reference Lib. Guild, supra [where the petitioner was unable to prove, given the circumstances, that holding all sales taxable was an unreasonable audit methodology]).

Next, we turn to the issue of the Administrative Law Judge's determination that petitioner included sales tax in the price of his items, and that the Division overstated petitioner's sales prices.

20 NYCRR 532(b)(3) provides that when a customer is given, inter alia, any sales slip or receipt of the price paid or payable, the sales tax must be "stated, charged, and shown separately on the first of such documents," and that the words "tax included" or words to that effect on the sales slip or receipt are not sufficient to constitute a "separate statement" of the tax, so that the total amount charged is deemed to be the sales price only. However, it has long been the recognized policy of the Division that where no written receipt is given to a customer, a business establishment can include sales tax in the sales price of the item (the so-called "unit price" method) as long as the customer is made aware of the inclusion of sales tax in the sales price by visibly displaying a placard to that effect to all customers (20 NYCRR 532[b][4]; see, Advisory Opn, State Tax Commn., March 6, 1981 [TSB-H-81(56)S, March 23, 1981]; TSB-M-79[15]S, December 3, 1979; cf., Matter of LaCascade, Inc. v. State Tax Commn., supra [unit price method held inapplicable where taxpayer gave each of its customers a written receipt]). The Administrative Law Judge found credible petitioner's testimony that "[i]n front of the store we have a price that says 'sales tax included'" (Tr., p. 62) in the sales price in conformity with 20 NYCRR 532(b)(4). In contrast, the Administrative Law Judge did not find credible the

auditor's testimony. The auditor testified that she visited only one of the two stores in question (Tr., p. 55), and ultimately explained that she saw prices posted which did not indicate that sales tax was included (Tr., p. 48). However, the auditor had first stated that she didn't know whether the prices she listed as petitioner's selling prices included sales tax. Therefore, the Administrative Law Judge was not convinced that petitioner did not have a sign at his stores indicating that sales tax was included in the sales prices.

On questions of credibility of a witness, it is our policy not to disturb the analysis of the Administrative Law Judge barring compelling reasons (see, Matter of Constantino, Tax Appeals Tribunal, September 27, 1990). Despite the Division's attempt to explain away the apparent contradiction in the auditor's testimony (see, Division's brief on exception, p. 5, footnote 3), we are not swayed by this argument and, therefore, defer to the Administrative Law Judge's determination that petitioner had indeed posted the required notice regarding sales tax and that, therefore, the prices posted should not have been further inflated to account for additional sales tax.

We turn now to the issue of the Administrative Law Judge's reduction in the taxable use percentage applied to small dishes and sugar cones. Petitioner proved that the reductions sought, namely from 100% to 5% for the percentage of taxable use of sugar cones[15] and from 100% to 30% for the taxable use of small dishes, were proper, based on his credible testimony as found by the Administrative Law Judge. The testimony that petitioner used these items mostly in the creation of take-home, nontaxable desserts was persuasive to the Administrative Law Judge, and we see no compelling reason to overturn his findings or ultimate decision on the issue.

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[15]We note that we agree with the Division's claim in its brief on exception that the Administrative Law Judge erroneously stated in conclusion of law "E" that the taxable use of sugar cones is to be reduced from 95% to 5%, rather than from 100% to 5% (Division's brief on exception, p. 2, footnote 1). Petitioner's Exhibit "4," which purportedly lists the discounts allotted petitioner by the Division, includes a discount of 5% for sugar cones, for a taxable rate of 95%. However, petitioner's Exhibit "2," as reproduced in the Administrative Law Judge's finding of fact "5," reveals that, the auditor had assessed petitioner based on a 100% taxable use figure for sugar cones, and had not consented to a 95% taxable use figure. Accordingly, we hereby correct the Administrative Law Judge's statement in conclusion of law "E" to read: "Therefore, a reduction from 100% to 5% for the percentage of taxable use of sugar cones is proper."

Likewise, we see no reason to overturn the Administrative Law Judge's rulings regarding petitioner's proposed reductions in taxable use percentages applied to small and large (non-sugar) cones, egg cream cups and 1/2 pint containers. Petitioner has not required us to review these issues by filing a timely exception (see, Matter of Armel, supra; Matter of Klein's Bailey Foods, supra; Matter of Caleri, supra), and we see no reason to exercise our discretion under 20 NYCRR 3000.11(e) to review them.

Accordingly, it is ORDERED, ADJUDGED, and DECREED that:

1. The exception of the Division of Taxation is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petition of Frank Auriemma is granted to the extent indicated in the Administrative Law Judge's conclusions of law "C," "D" and "E," but is in all other respects denied; and

4. The notices of determination and demand for payment of sales and use taxes due dated August 21, 1987 are modified, in accordance with paragraph "3" above, but are otherwise sustained.

DATED: Troy, New York
September 17, 1992

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

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

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