STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
NEGAT, INC. **AND ARAYA SELASSIE, AS OFFICER**	:	DECISION DTA No. 806881
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 June 1, 1984 through February 28, 1987.	:	

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on March 14, 1991 with respect to the petition of Negat, Inc. and Araya Selassie, as officer, 5 Dean Court, Rutherford, New Jersey 07070 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 June 1, 1984 through February 28, 1987. Petitioners appeared by William P. Maloney, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Patricia L. Brumbaugh, Esq., of counsel).

Each party filed a brief on exception. Oral argument, at the request of the Division of Taxation, was heard on October 10, 1991.

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

ISSUES

I. Whether the notices of determination issued to petitioners were jurisdictionally defective because they failed to indicate that the tax assessed was estimated as provided for in Tax Law § 1138(a)(1) and, therefore, invalid.

II. Whether the method of audit selected by the Division of Taxation was reasonably calculated to reflect the tax due.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "5" which has been modified. The Administrative Law Judge's findings of fact and the modified finding of fact are set forth below.

Petitioner, Negat, Inc., operated a restaurant on the second floor of a building located at 2628 Broadway in New York City. An audit of Negat wastriggered by Negat's filing of a notification of a bulk sale with the Division of Taxation ("Division").

Negat mailed a form entitled "Notification of Sale, Transfer or Assignment in Bulk" to the Division by United States Postal Service certified mail. The postmark on the envelope in which the form was mailed is April 5, 1987. It was date stamped by the Division's Administration Section on April 10, 1987 and by the "Sales Tax" section on April 13, 1987. The notification indicated that on November 5, 1986 Negat sold a restaurant to Bahama Mama, Inc. for a total selling price of $20,000.00, of which $5,000.00 was allocated to furniture, fixtures and other tangible personal property. A sales tax of $412.50 was remitted. The form is signed by Araya Selassie and dated November 5, 1986.

On or about April 16, 1987, the Division issued to Bahama Mama a notice of a possible claim for sales tax due. The notice instructed Bahama Mama not to release any funds or property until authorized to do so. On or about the same date, a similar document was issued to Negat's escrow agent. On or about May 7, 1987, the Division issued a notice to Negat (addressed to Negat, care of Bahama Mama), advising that an examination of Negat's books and records might be scheduled in the future.

On May 28, 1987, a district office was assigned to audit the sales tax records of Negat. Through contact with Negat's escrow agent, the Division identified Araya Selassie as a principal of Negat and received Mr. Selassie's home address and telephone number. A letter was sent to Mr. Selassie, dated June 5, 1987, asking Mr. Selassie to telephone the tax auditor conducting this audit, and on June 15, 1987, Mr. Selassie called the auditor. The auditor explained to Mr.

Selassie that the Division would need Negat's sales records for the audit period in order to conduct an audit. Mr. Selassie stated that he would have Negat's accountant, Joel L. Pogolowitz, contact the auditor. On June 16, 1987, Mr. Pogolowitz did in fact telephone the auditor who was not then available. Two telephone conversations followed between Mr. Pogolowitz and the auditor. On June 17, 1987, Mr. Pogolowitz informed the auditor that he was attempting to gather Negat's business records from Mr. Selassie. On July 7, 1987, Mr. Pogolowitz told the auditor that Mr. Selassie had been unable to provide the requested records because his wife was in the late stages of a difficult pregnancy and Mr. Selassie was flying back and forth between New York and England to be with her.

We modify finding of fact "5" of the Administrative Law Judge's determination to read as follows:

> Because books and records were not available and the 90-day period of limitation for assessment of tax against Bahama Mama was due to expire, the Division decided to estimate Negat's sales tax liability. The auditor's supervisor visited Bahama Mama (the date and time of the visit are not in the record) and noted that it was a restaurant with a sit-down bar. The record does not indicate whether the restaurant was open or whether there were any customers present at the time of the observation. From a conversation with a bookkeeper, he concluded that Bahama Mama's "business was same type as the previous business - except that a new decor set up" (audit workpapers, p. 4). The record does not reveal any basis to infer that the bookkeeper was familiar with the operations of Negat's restaurant. The auditor confirmed, through the Division's records, that Bahama Mama registered as a sales tax vendor as of December 1986 and filed sales tax returns for the periods December 1, 1986 through February 28, 1987, and March 1, 1987 through May 31, 1987. According to the auditor's workpapers, Bahama Mama reported taxable sales of $132,046.00 for "the first full quarter" (referring to the period ended May 31, 1987).[1]

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[1]The Administrative Law Judge's finding of fact "5" read as follows:

> "5. Because books and records were not available and the 90-day period of limitation for assessment of tax against Bahama Mama was due to expire, the Division decided to estimate Negat's sales tax liability. The auditor's supervisor visited Bahama Mama (the date and time of the visit are not in the record) and noted that it was a restaurant with a sit-down bar. From a conversation with a bookkeeper, he concluded that Bahama Mama's "business was same type as the previous business - except that a new decor set up" (audit workpapers, p. 4).
>
> (continued...)

Based on Bahama Mama's reported taxable sales and the observation of the audit supervisor, the Division estimated that Negat had taxable sales of $10,000.00 per week (or $130,000.00 per sales tax quarter) for the period June 1, 1984 through February 28, 1987, with a sales tax liability of $10,725.00 per sales tax quarterly period. To determine tax due, the Division subtracted sales taxes paid by Negat for each quarter included in the assessment period from the estimated tax due. This resulted in total sales tax due of $112,116.03.

The Division mailed two notices of determination and demands for payment of sales and use taxes due, dated July 13, 1987, to petitioner Negat, Inc. The first notice assessed sales tax due for the period June 1, 1984 through February 28, 1987 in the amount of $112,116.03 plus penalty and interest. The second notice assessed an additional penalty of $7,414.13 for the period June 1, 1985 through February 28, 1987. Notices dated July 13, 1987 were also issued to Araya Selassie as officer of Negat, Inc., assessing identical amounts of tax, penalty and interest.[2]

Each of the notices of determination issued contain the following statements, preprinted in bold-faced type:

> "The tax assessed above has been estimated in accordance with the provisions of section 1138(a)(1) of the Tax Law." [This statement was preceded by a box.]
> "If the box above is checked see additional information on back of this notice. If the box above is not checked, the tax has not been estimated.

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[1](...continued)
The auditor confirmed through the Division's records that Bahama Mama registered as a sales tax vendor as of December 1986 and filed sales tax returns for the periods December 1, 1986 through February 28, 1987 and March 1, 1987 through May 31, 1987. According to the auditor's workpapers, Bahama Mama reported taxable sales of $132,046.00 for "the first full quarter" (referring to the period ended May 31, 1987).

We modified this fact to reflect more details of the record.

[2]The notices issued to petitioners most probably were issued after the expiration of the 90-day period of limitation for assessment of tax found at Tax Law § 1141(c). The auditor's contact sheet indicates that the notices of determination were prepared on July 13, 1987, 94 days after the Division received the notification of sale from Negat and 99 days after the notification was mailed to the Division. However, the time requirements of Article 28 have been held to constitute a statute of limitations which must be pleaded as an affirmative defense (Matter of Servomation Corp. v. State Tax Commn., 60 AD2d 374, 400 NYS2d 887). As petitioners failed to raise this issue, they must be considered to have waived any claim they may have had in this regard (see, Matter of Convissar v. State Tax Commn., 69 AD2d 929, 415 NYS2d 305, 306; Matter of Jencon, Tax Appeals Tribunal, December 20, 1990).

The boxes referred to on the notices of determination were not checked on any of the notices.

The first notice of determination issued to Negat (S870713144M), which assessed tax, penalty and interest, contains this typewritten statement:

> "Since you have not submitted your records for audit as required by Section 1142 of the Tax Law, the following taxes are determined to be due in accordance with Section 1138 of the Tax Law."

The second notice of determination (S870713145M), which assessed only penalty, contains this typewritten statement:

> "The following penalties are being imposed pursuant to Section 1145 of the Tax Law and are based on the results of an audit of your records: This notice is in addition to Notice Number S870713144M."

An identical statement appears on the notice of determination issued to Mr. Selassie (S870713147M), assessing a separate penalty. The notice of determination issued to Mr. Selassie (S870713146M), assessing tax, penalty and interest for the audit period, contains this typewritten statement:

> "You are liable individually and as Officer of Negat, Inc. under Sections 1131(1) and 1133 of the Tax Law for the following taxes determined to be due in accordance with Section 1138(a) of the Tax Law."

All of the shares of stock of Negat were owned by Abdella Nour and another gentleman from the first day of the audit period until August 1985, when all shares of stock were purchased by Araya Selassie and Tadesse Shiferaw for $27,000.00. Because of disagreements between Mr. Nour and his partner, the restaurant was actually closed from June 1, 1984 through October 1, 1984.

The transfer of stock from Mr. Nour and his partner to Mr. Selassie and Mr. Shiferaw was not reported to the Division as a sale or transfer of business assets. Copies of sales tax returns filed by Negat for the sales tax quarters ended May 31, 1984 and August 31, 1984 were signed by Abdul Ahmed as president.

After the transfer of stock, Mr. Selassie continued to operate the restaurant in essentially the same manner as it had been operated by Mr. Nour. The restaurant was called Nayala; Ethiopian food, beer, wine and non-alcoholic beverages were served. The restaurant did not have a separate bar for serving customers. It was operated by three family members and one unrelated employee. It was open only during dinner hours, approximately 6:00 P.M. to 11:00 P.M., seven days per week. Mr. Selassie began operating Nayala in July 1985 and then closed the restaurant for renovations. He reopened on August 18, 1985. In June and July 1986, Mr. Selassie's wife was ill as the result of a difficult pregnancy, and she eventually suffered a miscarriage. Because he was traveling between America and England to be with his wife, Mr. Selassie began operating the restaurant on a less regular basis. In June 1986, the restaurant was open six days per week, and in July 1986 it was open only three to five days per week.

Negat used individual guest checks to record its sales. Petitioner offered into evidence guest checks for the period August 18, 1985 through July 18, 1986. These were sequentially numbered and arranged by date. Each guest check separately stated food items, beverages, a sub-total, the tax charged on the sub-total amount and a total. Totals taken from the guest checks were posted to ledger sheets in the following categories: sales, tax and total. Expenses were also posted to the same set of ledger sheets. The ledger sheets were also entered into evidence, and a random review of the guests checks and ledger sheets failed to reveal any error in postings. Because of his wife's illness, Mr. Selassie made no entries on the ledger sheets in June and July 1986.

An accountant employed by Negat to represent it in matters involving the instant audit totaled the guest checks and determined tax due for the period July 27, 1985 through July 18, 1986 of $5,100.00.[3] Negat paid sales tax for the period June 1, 1985 through August 31, 1986 of $404.52. The accountant testified that Negat did not accurately report its taxable sales during this period.

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[3]By dividing 1.0825 into $5,100.00, it can be determined that the accountant calculated taxable sales of $61,818.18. An independent review of the guest checks verified this result.

Mr. Selassie closed the restaurant in July 1986 and entered into negotiations for the sale of the business. The Division had in its files a contract of sale between Negat and Bahama Mama, dated September 12, 1986. It is not known how or when the contract came into the Division's possession. The contract indicates that the purchase price of the business was to be $20,000.00 and was to include the sale of any open stocks of beer, wine, alcohol, soft drinks and food. By the terms of the contract, Negat obligated itself to secure the written consent of the landlord to the assignment of Negat's lease and security to Bahama Mama and to negotiate a new lease satisfactory to Bahama Mama. In the event that Negat was unable to secure the landlord's consent to the assignment, the sales contract was to be deemed null and void. Although the date of closing shown in the lease was October 15, 1986, negotiations with Negat's landlord delayed the actual closing until November 1986. The final purchase price was $24,000.00. A schedule attached to the contract indicates that the following property was transferred in the sale:

Tables	Freezer	Glasses
Chairs (about 35)	Hot water heater	Cups
Service Bar	Air Conditioner	Kitchen Utensils
4 Burner Stove	Gas Heating System	Fire Extinguishers
3 woks	Glass Display Case	Emergency Lights
Walk-in Refrigerator	Steam Table	Metal Sinks
Low Refrigerator	Food Warmer Shelf	Glass Door Refrigerator
Cash register	Office Desk	

Bahama Mama executed a consent agreement with the Division whereby it accepted liability for taxes determined to be due from Negat for the audit period, up to and including the final purchase price. Mr. Selassie testified that the final amount was $24,000.00. The parties agreed that any amounts paid by Bahama Mama as a consequence of the consent agreement would be applied to Negat's sales tax liability.

The operation of Bahama Mama differed from that of Nayala. Bahama Mama served liquor, as well as beer and wine, and had a sit-down bar along with table service. Bahama Mama totally renovated the restaurant, adopting a tropical decor and serving Caribbean type food. Neither party offered any evidence of the operating hours of Bahama Mama or prices charged.

A conciliation order, dated February 3, 1989, sustained the statutory notices issued to Negat and Mr. Selassie and denied their requests for redetermination of the tax assessments. The

books and records offered into evidence at this hearing were made available to the Division at that conference; however, they were not reviewed by the Division at that time.

The Negat auditor testified that at the time of this audit he had been employed by the Division for almost ten years and prior to this audit had conducted five to eight audits of restaurants and had cooperated in the audits of eight to ten other restaurants. He gave no further details with regard to his experience in auditing restaurants, nor did he specifically relate this experience to his audit of Negat.

OPINION

The Administrative Law Judge determined that the failure of the Division to check the box on the notices of determination to advise petitioners that the tax was estimated, rendered the notices of determination assessing tax invalid. The Administrative Law Judge determined that even if the estimated assessment notice was only required where the taxpayer did not otherwise have such notice, the notice would be required here, because the Division did not communicate to petitioners the nature of the estimating techniques used until well after the issuance of the notices. The Administrative Law Judge rejected the Division's contention that the lack of a checkmark on the form was cured by the typewritten advisory information placed on each notice of determination, concluding that the typewritten information neither informed petitioners that the tax due was estimated nor complied with the requirements of section 1138(a)(2) of the Tax Law. Since the notices assessing tax were invalid, the Administrative Law Judge determined that the notices of determination assessing penalties must also be cancelled.

Although she concluded that the notices of determination were invalid, the Administrative Law Judge addressed the underlying audit, in order to create a complete record for review. With respect to this audit, the Administrative Law Judge found that the Division properly resorted to external indices to estimate the tax because petitioners failed to timely respond to the Division's request for books and records. However, the Administrative Law Judge held that the external index utilized, sales by a subsequent restaurant in the same premises, was not a method reasonably calculated to estimate the taxes due. The Administrative Law Judge also determined

that Mr. Selassie's purchase of the stock of Negat did not constitute a business asset of Negat and, therefore, did not trigger the bulk sale provisions of the Tax Law. Further, the Administrative Law Judge held that Mr. Selassie was not personally liable, as a responsible officer, for the taxes of Negat until July of 1985. Finally, the Administrative Law Judge concluded that petitioners did not have standing to request a refund of taxes paid by Bahama Mama.

In its exception, the Division argues that the Administrative Law Judge erred in allowing petitioners to raise the section 1138(a)(2) argument in their post-hearing brief. The Division asserts that to allow this argument to be raised for the first time, after the hearing, violates 20 NYCRR 3000.4, which prohibits the amendment of a pleading to raise a point of controversy barred by the statute of limitations, unless the original pleading gave notice of the point in controversy. The Division also argues that section 1138(a)(2) does not require a specific size type, nor the use of the term "estimated" and, thus, reasserts its contention that the typewritten statement on the form satisfied the statutory requirement. The Division asserts that the Administrative Law Judge's reliance on case law arising under section 313(1) of the Vehicle and Traffic Law was misplaced because that statute had the goal of protecting the innocent injured party. The Division also argues that the legislative history surrounding section 1138(a)(2) indicates that its purpose was to "enhance the knowledge of the taxpayer with respect to its right to a hearing" (Division's brief, p.11). With respect to the audit methodology employed, the Division argues that the use of audit experience was reasonable because it was the only method available, given the late submission of the Bulk Sale Notice and the failure of petitioners to make records available at the time of the audit. The Division contends that the estimate based on audit experience was verified by the comparison to the sales of the bulk purchaser for its first full quarter of business.

In response, petitioners argue that the typewritten statement on the notice could not satisfy section 1138(a)(2) because, even assuming that the statement stands out, it is contrary to the statement on the form that provides that if the box is not checked, the tax is not estimated.

Petitioners also argue that the typewritten statement does, borrowing the Division's phrase, require a quantum leap in logic for the taxpayer to conclude that the tax was estimated. Such a leap is inappropriate, assert petitioners, in the face of a statute that is intended to protect the legal rights of the reader of the notice. Petitioners also contend that the case of Matter of Nassau Ins. Co. v. Hernandez (65 AD2d 551, 408 NYS2d 956) cannot be validly distinguished from the instant case because "the point is notice, and the view of the Courts of this State with regard to notice" (petitioners' brief on exception, p. 4). Next, petitioners disagree with the Division's interpretation of the legislative history surrounding section 1138(a)(2), arguing that this material indicates that section 1138(a)(2) was meant to provide taxpayers with the right to know the manner in which the determination of tax was reached, as well as to provide the taxpayer with notice of the right to contest the determination. Petitioners also argue that to prohibit it from raising the issue in its post-hearing brief would not be in the interests of justice because the notices "would seem to be the heart of the matter" (petitioners' brief on exception, p. 8). Petitioners contend that they should be allowed to raise this issue because the contents of the notices were undisputed and the Division was given the opportunity to reply to the new issue in its post-trial brief. With respect to the audit performed, petitioners acknowledge that the Division had the right to utilize external indices to estimate tax, but assert that the method chosen was not reasonably calculated to estimate the sales tax liability. Petitioners state that the method utilized by the auditor, i.e., a comparison to the new operation, was simply a guess and that petitioners have demonstrated that this method, and its results, were erroneous.

We address initially the Division's assertion that the Administrative Law Judge erred in concluding that the failure to indicate on the notices of determination that the tax assessed was estimated, constituted a jurisdictional defect invalidating the assessment.

The first subset of this issue is whether the Administrative Law Judge erred in allowing petitioners to raise the issue for the first time in their post-hearing memorandum of law.

We affirm the Administrative Law Judge.

The absence of a valid assessing document is jurisdictional in nature, which precludes a determination as to the correctness of the amount of tax imposed, and more importantly, causes the assessment to be void (Matter of Scharff, Tax Appeals Tribunal, October 4, 1990; Matter of Malpica, Tax Appeals Tribunal, July 19, 1990).[4] Because the issue raised by petitioners calls into question the validity of the assessing document, we conclude that it could be raised at any time, provided the parties had adequate notice of the issue (New York State Dept. of Taxation & Fin. v. Tax Appeals Tribunal, Sup Ct, June 29, 1991, Keniry, J.). Since petitioners raised the issue in their post-hearing memorandum of law, to which the Division had adequate time to reply, there is no question of adequate notice to the parties.

We deal next with the issue of whether the Division's noncompliance with the provisions of Tax Law § 1138(a)(2) was a fatal defect invalidating the notice. We reverse the determination of the Administrative Law Judge.

Tax Law § 1138(a)(1) provides that if a sales tax return is incorrect or insufficient:

> "the amount of tax due shall be determined by the commissioner of taxation and finance from such information as may be available. If necessary, the tax may be estimated on the basis of external indices, such as stock on hand, purchases, rental paid, number of rooms, location, scale of rents or charges, comparable rents or charges, type of accommodations and service, number of employees or other factors."

In 1979, the Legislature amended section 1138 by adding subparagraph (2) to subdivision (a) (L 1979, ch 714). Section 1138(a)(2) provides that:

> "[w]henever such tax is estimated as provided for in this section, such notice shall contain a statement in bold face type conspicuously placed on such notice advising the taxpayer: that the amount of the tax was estimated; that the tax may be challenged though a hearing process; and that the petition for such challenge must be filed with the tax commission within ninety days" (emphasis added).

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[4]Our decision in Matter of Scharff was later vacated by the Supreme Court; however, the ground for the court's decision was that we had failed to give notice to the parties before we concluded, on our own motion, that we lacked subject matter jurisdiction (New York State Dept. of Taxation & Fin. v. Tax Appeals Tribunal, Sup Ct, June 29, 1991, Keniry, J.). Therefore, our conclusion that the absence of a valid assessing document is a jurisdictional defect that results in no assessment was not questioned by the court and remains unimpaired.

The notices at issue here apprised petitioners of the amount of tax assessed; that the tax could be challenged through a hearing process; and that a petition for such challenge had to be filed within 90 days. Contrary to the Division's assertion, the notices did not indicate that the tax was estimated.[5]

The crux of the matter is whether the language of section 1138(2), i.e., the notice "shall contain a statement in bold face type conspicuously placed on such notice advising the taxpayer: that the amount of the tax was estimated . . ." (emphasis added) is mandatory, as urged by petitioners, meaning that compliance with it is a condition precedent to the validity of the Division's action pursuant to the section (see, People v. Alejandro, 70 NY2d 133, 517 NYS2d 927, 931); or is the language directory, as urged by the Division, meaning that it is intended by the Legislature not to be disobeyed, but a disregard of it, or an inexact compliance, will constitute only an irregularity, not a fatal defect (McKinney's Con Laws of NY, Book 1, Statutes § 171).

The task is one of statutory construction and interpretation. The difficulty always is in reconciling a different result from that which would ordinarily flow from the clear mandatory language of a statute. There is no absolute test (82 CJS § 376). As stated in Matter of King v. Carey (57 NY2d 505, 457 NYS2d 216):

> "the line between mandatory and directory statutes cannot be drawn with precision [citations omitted]. The inquiry involves a consideration of the statutory scheme and objectives to determine whether the requirement for which dispensation is sought by the government may be said to be an 'unessential particular' [citations omitted] or, on the other hand, relates to the essence and substance of the act to be performed and thus cannot be viewed as merely directory [citations omitted]."

While the Legislature's use of terms such as "must" or "shall" is not conclusive, such words of command are ordinarily construed as peremptory in the absence of circumstances suggesting a contrary legislative intent (see, Escoe v. Zerbst, 295 US 490, 493; People v. Schonfeld, 74 NY2d 324, 547 NYS2d 266, 267). "Whether a given provision in a statute is mandatory or directory is

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[5]The preprinted box on the notices, which was to be checked in the event that the assessment was estimated, was not checked. Contrary to the assertion of the Division, the typewritten statements on the notice did not advise petitioners that the tax due was estimated. The statements merely referred to section 1138 of the Tax Law which, as noted above, provides that taxes may be determined on the basis of either the books and records of the taxpayer or estimated on the basis of external indices.

to be determined primarily from the legislative intent gathered from the entire act and the surrounding circumstances, keeping in mind the public policy to be promoted and the results that would follow one or the other conclusion" (McKinney's Cons Laws of NY, Book 1, Statutes § 171; People v. Alejandro, supra; People v. Schonfeld, supra; People v. Graves, 277 NY 115).

We turn then to the legislative history of the statute. Subparagraph 2 of section 1138(a) was added along with other amendments to the Tax Law in a bill that became known as the "Taxpayer's Bill of Rights" (Memorandum of the Division of the Budget, Buffalo Evening News [June 30, 1979, B-2], Governor's Bill Jacket, L 1979, ch 714). The purpose of the bill was "to enact certain procedural reforms concerning the administration of sales tax" (Memorandum of Sen. Fred J. Eckert, 1979 NY Legis Ann, at 432). As stated by the bill's sponsor, Senator Eckert, "[t]his bill will assure certain taxpayers and vendors rights [and will] provide more information and certainty concerning their respective tax liability and hearing procedures . . ." (emphasis added).

Specifically, the bill was intended to "give taxpayers a more predictable environment in which to operate . . . [and that] [t]o further inform taxpayers, the bill calls for clearer notification of taxpayers, alerting them to the nature of the assessment and the rights of the assessed" (Memorandum of Division of Budget, Governor's Bill Jacket, L 1979, ch 714, emphasis added).

The Commissioner of Taxation and Finance, in his comments to the Governor's Counsel after the bill had been passed by the Legislature and was awaiting executive action, was generally supportive of the legislation, but expressed the reservation that "[t]he proposed amendment should be clarified to exclude estimated assessments based on audits when the taxpayer would be aware of any estimating techniques used" (Governor's Bill Jacket, L 1979, ch 714).

We find nothing in this legislative history which supports the conclusion offered by petitioners and embraced by the dissent that the Legislature intended that a failure of exact compliance with the language of the statute to be a fatal defect which renders the notice invalid. Indeed, we find such a result drastic and somewhat unrealistic in that it would have us conclude, in effect, that the Legislature intended that the validity of the entire process depended on the

Division's compliance with but one single requirement of section 1138(2). On the contrary, it is clear that the Legislature's expressed intention was to insure that taxpayers were informed of the nature of the assessments against them so that they could properly respond to those assessments through the protest procedures provided to them. It is also abundantly clear that the Division's failure to "check the box" on the notice, thereby indicating that the assessment was estimated, did not frustrate the plan of the Legislature to safeguard petitioners' rights.

The record here shows that petitioners were aware that the Division was engaged in an audit of their business activities; that the Division requested petitioners' books and records for purposes of the audit; and that petitioners did not provide the Division with their books and records from which an audit could be conducted. The petitioners' petition indicates that petitioners were aware of the fact that the assessment was estimated and challenged the assessment on the basis that such audit methodology was wrongly applied in petitioners' case (see, Exhibit "E," ¶¶ "3" and "9").

In short, petitioners were not misled or prejudiced and enjoyed every privilege which a formally correct notice would have given them. This result is consistent with the rationale of the court in Matter of Mon Paris Operating Corp. v. Commissioner of Taxation & Fin. (Sup Ct, Albany County, March 16, 1988, affd on other grounds 151 AD2d 822, 542 NYS2d 61) where the identical issue was dealt with by the Supreme Court in its decision. The Court in Mon Paris held that the Division's failure to indicate that the tax was estimated did not invalidate the assessment. Rather, it held that a taxpayer must be prejudiced by this omission in order to invalidate the notice. Finding that the petitioner was aware of the estimated nature of the tax and of his need to pursue a remedy, the court concluded that no prejudice existed (Matter of Mon Paris Operating Corp. v. Commissioner of Taxation & Fin., supra;[6] see also, Matter of Pepsico,

[6]In Mon Paris, the taxpayer brought an action under Article 78 commenced in Supreme Court, Albany County, seeking a refund of taxes allegedly demanded unlawfully by a notice of determination. The Division moved to dismiss the petition, claiming the taxpayer had failed to utilize its administrative remedies and that this failure resulted in the tax becoming finally and irrevocably fixed. The Appellate Division, in affirming the Supreme Court, did not deem it necessary to address the issue of the validity of the assessment, but affirmed on the grounds that the taxpayer's payment of tax under the Amnesty Program constituted admission of tax due, thus, making it "unnecessary

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Inc. v. Bouchard, 102 AD2d 1000, 477 NYS2d 892 [notice misstating the period for which tax assessed not invalid since taxpayer not prejudiced]; Matter of Tops, Inc., Tax Appeals Tribunal, November 22, 1989 [two sales tax quarters incorrectly listed on the statutory notice did not render it invalid]). The result here is also consistent with those cases which deal with the mandatory requirement that the notice of deficiency be mailed to the taxpayer's "last known address" (Tax Law § 681[a]; Matter of Agosto v. State Tax Commn., 68 NY2d 891, 508 NYS2d 934; Matter of Riehm, ___AD2d___ [January 30, 1992]). The persuasive fact in each case was that the taxpayer received the notice even though improperly addressed by the Division. In rejecting a strict construction of the word "shall" contained in section 681(a), these cases were grounded upon the legislative history of section 681(a), which stated that the purpose of its enactment was to bring New York in conformity with the comparable Federal provision, Internal Revenue Code § 6212(a) and (b). In accordance with this legislative directive, both cases followed Federal case law in reaching their decisions.

Turning to the merits of the audit, we agree with the Administrative Law Judge that the estimate method used by the Division did not have a rational basis. As set forth in the facts, the methodology consisted of a visit to the restaurant as operated by Bahama Mama, Inc. The audit supervisor determined that the sales of the two restaurants were similar based on a discussion with a bookkeeper at Bahama Mama. Based on the sales reported by Bahama Mama for the first full quarter of its operation, the Division estimated Negat's sales. The Division describes this method as "the use of [the auditor's] substantial experience with respect to the dollar amount of sales which could reasonably be expected of a restaurant of the type in question at that location" (Division's brief on exception, p. 18) and argues that it was reasonable because it was the only method available. While this may have been the only audit methodology available, it was not the methodology employed by the Division, because we find nothing to indicate that the Division ascertained the type of restaurant operated by Negat.

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[6](...continued)
to reach the other grounds the Supreme Court relied on for affirmance."

A source of the Division's information about the Negat restaurant was the bookkeeper at Bahama Mama. However, there is nothing in the record to indicate that the bookkeeper had any knowledge of the operation of the restaurant by Negat, or that the audit supervisor had any reason to believe that the bookkeeper had such knowledge. The court in Matter of Grecian Sq. v. New York State Tax Commn. rejected an estimate based on audit experience where that experience consisted of a comparison to other undescribed businesses (Matter of Grecian Sq. v. New York State Tax Commn., 119 AD2d 948, 501 NYS2d 219, 221). If the undescribed experience of an auditor does not provide a rational basis for an audit, certainly a comparison founded on the undescribed experience of a person identified only as the bookkeeper of the purchaser of the business does not.

Apart from the comparison obtained from the bookkeeper, the only other basis that the Division had to determine the "type" of Negat's business was the information acquired by the Division about the business, which was practically nothing. The Division did not know the type of food served by petitioners, whether petitioners served liquor, the number of employees in the restaurant or the physical arrangement of the premises (Hearing Tr., pp. 52-53). Further, the Division had extremely limited information about the characteristics of Bahama Mama, other than the bookkeeper's comparison to Negat's restaurant. Although the auditor's supervisor saw the premises, the record does not indicate that he actually observed the restaurant in operation or knew any details of the business, e.g., number of employees, hours of operation, amounts of purchases or the number of customers. The record does indicate that the auditor did not know what type of food was served by Bahama Mama (Hearing Tr., p. 59) and was not certain that Bahama Mama sold liquor (Hearing Tr., p. 53). The basis for the Division's comparison of Negat's restaurant to Bahama Mama was simply that the two businesses were restaurants located in the same premises (Hearing Tr., pp. 53, 59). We do not find this to be a rational basis to assume that the two businesses were similar (see, Matter of Basileo, Tax Appeals Tribunal, May 9, 1991; Matter of Fokos Lounge, Tax Appeals Tribunal, March 7, 1991).

Accordingly, the audit methodology employed in this case consisted only of the undescribed experience of the bookkeeper and the auditor's comparison of two unknown entities. Although "[c]onsiderable latitude is given an auditor's method of estimating sales under such circumstances as exist in the case," there must still be a rational basis underlying the audit (Matter of Grecian Sq. v. New York State Tax Commn., supra, 501 NYS2d 219) and we conclude that none exists here.

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 modified;

3. The petition of Negat, Inc. and Araya Selassie, as officer, is granted; and

4. The notices of determination and demand dated July 13, 1987 are cancelled.

DATED: Troy, New York
April 9, 1992

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

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

Concurring Opinion in the Matter of the Petition of

NEGAT, INC. AND ARAYA SELASSIE, AS OFFICER

Francis R. Koenig (concurring):

I concur in the result reached by the majority to cancel the assessment, but dissent from their holding that the Division's failure to comply with section 1138(a)(2) of the Tax Law does not render the notice of determination invalid.

The essence of the majority's decision is that in enacting the language "whenever such tax is estimated . . . such notice shall contain a statement in bold face type conspicuously placed on such notice advising the taxpayer: that the amount of the tax was estimated" (Tax Law § 1138[a][2], emphasis added), the Legislature intended this statutory direction to be mandatory only when the taxpayer did not otherwise have notice of the fact that the assessment was based on an estimated audit. In my opinion, this conclusion is inconsistent with the language of the enactment, as well as with the case law applying other statutes that prescribe the contents of other required notices.

First, if the Legislature had only meant to require the Division to notify the taxpayer that the tax was estimated, and was not concerned about the precise form of the notification, the Legislature would have enacted a provision that simply required the Division to notify the taxpayer and would not have explicitly prescribed the form that the notification would take. By explicitly describing the form of the notice, section 1138(a)(2) indicates to me that the Legislature did not intend the notification of the estimated assessment to be left to the vagaries of the audit or, as here, the post-audit process. Instead, the Legislature intended that the taxpayer be informed in a certain way (on the notice of determination) and in a definite manner (bold type, conspicuously placed).

That this was the intention of the Legislature is underscored by the legislative history material cited by the majority: "[t]his bill will assure certain taxpayers and vendors rights, [and will] provide more information and certainty concerning their respective tax liability and hearing

procedures" (Memorandum of Senator Fred J. Eckert, 1979 NY Legis Ann, at 432, emphasis added); the bill was intended to "give taxpayers a more predictable environment in which to operate . . . the bill calls for clearer notification of taxpayers, alerting them to the nature of the assessment" (Memorandum of Division of Budget, Governor's Bill Jacket, L 1979, ch 714, emphasis added).

The majority decision undermines this legislative goal of certainty, predictability and clarity because it allows the Division to issue a notice of determination that states that the tax was not estimated, and to overcome this error based on information obtained by the taxpayer from an unknown source, at some point prior to the filing of the petition. A taxpayer who is the recipient of this absolutely contradictory information then has the burden, under the majority's view, to show that he has been harmed by this misinformation. In my view, this is exactly the type of situation the Legislature sought to avoid when it directed the Division, through the enactment of section 1138(a)(2), to give notice of an estimated assessment in a certain, clear manner.

Although, as noted by the majority, there is nothing in the legislative history that explicitly states that the failure to comply with section 1138(a)(2) of the Tax Law renders the notice of determination a nullity, case law indicates that such an explicit statement is not necessary to give "shall" its normal mandatory meaning.

In Parker v. Mack (61 NY2d 114, 472 NYS2d 882), the plaintiffs sought to commence a civil action by serving upon the defendant two summonses unaccompanied by complaints. Despite the requirement under CPLR 305(b)[7] that a default notice shall be attached to the summons, the papers served gave no notice of the relief sought. The New York Court of Appeals, focusing on the imperative language of CPLR 305(b), held that the failure to comply

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[7]CPLR 305(b) provides as follows:

> "Summons and notice. If the complaint is not served with the summons, the summons shall contain or have attached thereto a notice stating the nature of the action and the relief sought, and, except in an action for medical malpractice, the sum of money for which judgment may be taken in case of default" (emphasis added).

with the statutory notice requirements meant that no action was commenced. Responding to the dissent's contention that the treatment of this defect as jurisdictional should be limited to the effect of default judgments, the Court stated:

> "[w]ere such discrete - and unusual - consequences intended, the Legislature could readily have so provided. No such differentiation is evidenced in the statute however. In that circumstance, respect for legislative authority requires that we give equal effect for all purposes to the explicit addition of the imperative 'shall' in CPLR 305 [subd.(b)]" (Parker v. Mack, supra, 472 NYS2d 882, 883-884).

In Matter of Nassau Ins. Co. v. Hernandez (supra), the Appellate Division held that an insurer's failure to comply with the requirements of section 313(1) of the Vehicle and Traffic Law when issuing a notice of termination, rendered the notice invalid. Section 313(1) required a notice of termination to include a certain statement in 12 point type. In concluding that the use of 6 point type, rather than the required 12, rendered the notice invalid, the court stated:

> "[t]he requirement that 12 point type face be used is unambiguous and absolute, thereby indicating that there must be strict compliance with the statutory condition . . . . Therefore, proof that the defective notice may have been read and understood is irrelevant to the determination of whether the notice of termination is valid" (Matter of Nassau Ins. Co. v. Hernandez, supra, 408 NYS2d 956, 957; see also, In re Empire Mutual Ins. Co v. Malagoli, 133 AD2d 29, 518 NYS2d 803 [1st Dept 1987]; In re Aetna Cas. & Sur. Co. v. Morales, 70 AD2d 833, 418 NYS2d 17 [1st Dept 1979]; Cohn v. Royal Globe Ins. Co., 67 AD2d 993, 414 NYS2d 19 [2d Dept 1979], affd 49 NY2d 942, 428 NYS2d 881; Matter of Furstenberg v. Aetna Cas. & Sur. Co., 67 AD2d 580, 415 NYS2d 849 [1st Dept 1979], revd on other grounds 49 NY2d 757, 426 NYS2d 465).

Like the statutes involved in Parker and in Nassau Ins., section 1138(a)(2) describes the contents of a notice that is required to be given. In both Parker and Nassau Ins., it was held that strict compliance with the statute was required, without regard to whether actual notice was otherwise achieved, and that failure to comply rendered the notice invalid. In neither Parker nor Nassau Ins., did the court require explicit legislative history in order to give the term "shall" its total effect, i.e., to find the noncomplying notice a nullity.

I disagree with the comparison drawn by the majority between the instant question and that presented in both Matter of Agosto v. State Tax Commn. (supra) and Matter of Riehm (supra).

The issue in the latter cases was the effect of the Division's failure to comply with the statutory direction on how the method of notification was to take place, i.e., by mailing to the last known address. In my view, cases dealing with the method of notification (see also, Margeson v. Smith, 41 AD2d 896, 342 NYS2d 727) are distinct from the case before us which involves a statute that describes the contents of a notice. Where the statute describes in mandatory terms the contents of a notice, I believe it is inappropriate to inquire whether the recipient has been informed despite the noncomplying notice (see, Parker v. Mack, supra; Matter of Nassau Ins. Co. v. Hernandez, supra).

For similar reasons, I do not find the decision in Matter of Mon Paris Operating Corp. v. Commissioner of Taxation & Fin. (supra) persuasive. In holding that the notice of determination was valid, the Supreme Court, Albany County, rejected the taxpayer's argument that the Division's failure to check the estimate box invalidated the assessment. In so doing, the court relied on the holding of Matter of Pepsico, Inc. v. Bouchard (supra). This reliance on Pepsico appears to be misplaced because the court in Pepsico, dealing with the failure of a notice to set forth accurately the period of assessment, stated that "the statute mandating that notice be given does not prescribe the content of the notice . . . and, significantly, that the notice given . . . accomplished its purpose of apprising petitioner that sales and use taxes had not been paid . . ." (Matter of Pepsico, Inc. v. Bouchard, supra, 477 NYS2d 892, 893). In this case, as in Mon Paris, section 1138(a)(2) specifically requires that the notice of determination reveal the estimated nature of the assessment on its face.

For all of the foregoing reasons, I conclude that the failure to comply with section 1138(a)(2) of the Tax Law rendered the notice of determination invalid and that the assessment should be cancelled on this basis.

DATED: Troy, New York
April 9, 1992

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