

STATE OF NEW YORK  
TAX APPEALS TRIBUNAL

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In the Matter of the Petition :  
of :  
**CLONE ENTERPRISES, INC.** : DECISION  
and : DTA Nos. 807257,807259,  
BRUCE FILASKI, BRADLEY FILASKI, WILLIAM FILASKI : 807260 and 807261  
AS OFFICERS OF CLONE ENTERPRISES, INC. :  
for Revision of Determinations or for Refund :  
of Sales and Use Taxes under Articles 28 and 29 :  
of the Tax Law for the Period June 1, 1984 :  
through August 31, 1987 :

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The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on June 13, 1991 with respect to the petitions of Clone Enterprises, Inc. and Bruce Filaski, Bradley Filaski and William Filaski as officers of Clone Enterprises, Inc., 2193 Hillside Avenue, Bellmore, New York 11710 for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1984 through August 31, 1987. The Division of Taxation appeared by William F. Collins, Esq. (James Della Porta, Esq., of counsel). Petitioners appeared by Melvin Koenig.

The Division of Taxation filed a brief on exception. Petitioners did not respond. 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.

***ISSUE***

Whether the Administrative Law Judge erred in cancelling 4/7 of the assessment because she found no rational basis for the calculation of that portion of the assessment.

***FINDINGS OF FACT***

We find the facts as determined by the Administrative Law Judge except for finding of fact "8" which has been modified. We have also made an additional finding of fact. The Administrative Law Judge's findings of fact, the modified finding of fact and the additional finding of fact are set forth below.

On September 10, 1987, the Division of Taxation ("Division") issued to petitioner, Clone Enterprises, Inc. ("Clone"), a Notice of Determination and Demand for Payment of Sales and Use Taxes Due for the period June 1, 1984 through August 31, 1984, assessing tax due of \$13,582.64 plus penalty and interest. On the same date, notices of determination were issued to petitioners William Filaski, as secretary of Clone, Bruce Filaski, as president of Clone, and Bradley Filaski, as vice president of Clone, assessing tax, penalty and interest in the same amounts as those assessed against Clone.

On December 20, 1987, the Division issued two additional notices of determination to Clone. The first notice assessed tax in the amount of \$174,704.02 for the period September 1, 1984 through August 31, 1987 plus penalty and interest. The second notice assessed an additional penalty in the amount of \$13,433.93 for the period June 1, 1985 through August 31, 1987. Also on December 20, 1987, the Division issued two notices each to petitioners William Filaski, Bruce Filaski and Bradley Filaski, assessing tax, penalty, interest and additional penalties in amounts identical to those assessed against the corporation.

The audit at issue followed on the heels of an earlier audit of Clone for the period September 1, 1981 through May 31, 1984. During the earlier audit, Clone operated a disco named "Feathers" which served alcoholic beverages. On selected nights, Feathers operated a teen disco, selling only soda. In late December 1986, Feathers stopped selling alcoholic beverages and began operating strictly as a teen disco called W. W. Flash.

On April 24, 1987, an auditor called Clone's business telephone number and received a recorded message, stating that Clone was now operating a teen disco on Friday, Saturday and

Sunday nights. The message also stated that the business was offering home catering and provided a telephone number for that service. The auditor left a message on Clone's answering machine, asking Clone to call her. She then called the caterer's number and spoke to a woman named Jeannette. Jeanette stated that she saw the operators of the teen disco on weekends. The auditor asked Jeanette to have someone from Clone return her call, but no one did. The auditor called Clone's business telephone two more times and left messages on the answering machine asking to have her calls returned. She also sent Clone two short notes, which she called "flashers", that again asked Clone to contact her in connection with a sales tax audit. She received no communications whatsoever from Clone.

On or about June 12, 1987, the Division mailed an appointment letter to Clone, scheduling a field examination of all books and records pertaining to Clone's sales tax liability for the period June 1, 1984 through May 31, 1987. Clone was asked to make available for the Division's review all journals, ledgers, sales invoices, purchase invoices, cash register tapes, guest checks and bank statements maintained by Clone for the audit period. In addition, the letter requested completion of a bar fact sheet and questionnaire, information with regard to Clone's catering business and a record of booking reservations.

On June 29, 1987, the auditor went to Clone's place of business where she obtained Bruce Filaski's phone number and left a flasher asking Mr. Filaski to contact her. She called Mr. Filaski on June 30, 1987 and spoke to his brother Bill Filaski. She left a message asking Bruce Filaski to call her. On July 2, 1987, she called Bruce Filaski again, this time with some success. She advised him that the Division was conducting an audit of Clone's books and records. She was told that Clone's accountant, Melvin Koenig, was in Florida and unavailable for an audit. The auditor and Mr. Filaski discussed the possibility of having Mr. Koenig return to New York for the audit or of Clone's obtaining the services of a different accountant. Mr. Filaski stated that he would speak to Mr. Koenig.

On July 7, 1987, the auditor returned an earlier telephone call from Mr. Koenig. He informed her that he had just become aware of the audit and would not return to New York until

October. He asked that the audit be postponed until then. The auditor refused a postponement. She then asked Mr. Koenig to provide the Division with copies of Clone's Federal income tax returns for the audit years. Mr. Koenig declined to do so, stating that he would provide them in October when he returned.

Since the Division had no books and records to review, it decided to conduct an observation test to estimate Clone's sales tax liability. The test was performed by two auditors on Wednesday, August 26, 1987, from 7:30 P.M. to 1:00 A.M. The auditors made notes of their observation of the premises. The premises contained a bar with 22 bar stools and 8 sets of tables and chairs. They saw three video game machines and a cigarette machine. There were signs in the disco advertising live bands on Wednesday nights. In addition, there was an advertisement indicating that the disco could be booked for parties with catering by Jeanette and also that Clone arranged for home parties with complete catering and the services of a disc jockey and two assistants. The auditors saw three cash registers at the bar and one at the entrance. The auditors' notes indicate that the disco was open for business on Wednesday and Saturday nights.

One auditor stood at the entrance to the disco and physically counted customers entering the premises. Her count was divided into two categories, those paying the full price of \$12.00 and those possessing a V.I.P. card who paid a reduced admission fee of \$10.00. Total admission receipts of \$2,576.00 were computed based on the auditor's count. While standing at the entrance, the auditor noted that the cashier received phone calls from persons inquiring about renting the disco for parties. In addition several persons came in to view the premises with a view towards renting it for catered parties. A second auditor was stationed at the bar and counted the number of sodas sold at \$1.00 apiece. At the end of the evening, the auditor calculated soda sales of \$144.00. Total sales receipts were determined to be \$2,720.00.

We modify finding of fact "8" to read as follows:

Following the observation test, the auditor estimated Clone's sales tax liability for the period June 1, 1984 through August 31, 1984. The Saturday

night admission price was \$7.00 (\$1.00 off with a V.I.P. card)<sup>1</sup>, and the auditor assumed that the same number of customers went to the disco on Saturday nights as did on Wednesday nights. Thus, she calculated Saturday night admissions of \$1,416.00 and soda sales of \$144.00. The average of Wednesday and Saturday audited sales was \$2,140.00. A Newsday article published on July 15, 1987 notes at one point that W. W. Flash was open on Wednesdays, Fridays, and Saturdays, and at two other points in the article, lists Wednesdays, Saturdays and Sundays. The auditors' notes indicate that the disco was open for business on Wednesday and Saturday nights, however, the phone recording at petitioners' business stated that the disco was open on Friday, Saturday, and Sunday nights. As noted above, the observation test was performed on a Wednesday night. Also, the auditor knew that Clone provided catered parties at the disco and home catering but had no information with regard to the extent of the sales attributable to this business. Furthermore, the Division did not know when Clone stopped doing business as Feathers and began doing business strictly as a teen disco. The auditor assumed that sales of alcoholic beverages by Feathers would exceed soda sales by the teen disco. To account for these variables, she assumed that Clone did business seven days per week and had average daily sales of \$2,140.00. This was the basis for her calculation of audited quarterly taxable sales of \$194,740.00. To determine tax due from Clone, the auditor subtracted reported taxable sales from audited taxable sales and applied the sales tax rate to the difference. For the quarter ended August 31, 1984, these calculations resulted in a sales tax liability of \$13,382.64, and notices of determination assessing that amount were issued.<sup>2</sup>

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1

The auditor mistakenly allowed \$2.00 off with a V.I.P. card and did not recognize the error until preparing for the administrative hearing.

2

The Administrative Law Judge's finding of fact "8" read as follows:

"Following the observation test, the auditor estimated Clone's sales tax liability for the period June 1, 1984 through August 31, 1984. The Saturday night admission price was \$7.00 (\$1.00 off with a V.I.P. card)\*, and the auditor assumed that the same number of customers went to the disco on Saturday nights as did on Wednesday nights. Thus, she calculated Saturday night admissions of \$1,416.00 and soda sales of \$144.00. The average of Wednesday and Saturday audited sales was \$2,140.00. A Newsday article published on July 15, 1987 stated that W. W. Flash was open on Friday, Saturday and Sunday nights, as did a recorded message. Also, the auditor knew that Clone provided catered parties at the disco and home catering but had no information with regard to the extent of the sales attributable to this business. Furthermore, the Division did not know when Clone stopped doing business as Feathers and began doing business strictly as a teen disco. The auditor assumed that sales of alcoholic beverages by Feathers would exceed soda sales by the teen disco. To account for these variables, she assumed that Clone did business seven days per week and had average daily sales of \$2,140.00. This was the basis for her calculation of audited quarterly taxable sales of \$194,740.00. To determine tax due from Clone, the auditor subtracted reported taxable sales from audited taxable sales and applied the sales tax rate to the difference. For the quarter ended August 31, 1984, these calculations resulted in a sales tax liability of \$13,382.64, and notices of determination assessing that amount were issued."

\* The auditor mistakenly allowed \$2.00 off with a V.I.P. card and did not recognize the

We find an additional finding of fact to read as follows:

Aside from the lack of information regarding the extent of catering done and private parties hosted by petitioners, the record contains conflicting information as to which nights of the week the disco actually operated as a disco. Because all of the sources available concur that the disco operated on Saturdays, but conflict as to whether the other days of operation were Wednesdays, Fridays, or Sundays, and petitioners were unable to provide conclusive information in this regard, we find that the disco was open four days per week during the audit period.

After issuing the initial notices of determination, the Division continued its attempts to communicate with Clone's principals and accountant with regard to Clone's sales tax liability. Several phone calls were made to Mr. Koenig and to Bruce Filaski and flashers were mailed to Mr. Koenig in New York and in Florida. These attempts to contact Clone proved fruitless. Therefore, the Division determined Clone's sales tax liability for the period September 1, 1984 through August 31, 1987, using the methodology which it had employed to estimate tax due for the first sales tax quarter of the audit period.

Clone never provided the Division with any records or any information regarding its business practices. The Division obtained copies of Clone's 1983, 1984 and 1985 Federal income tax returns from the Internal Revenue Service after the notices of determination were issued. Petitioners placed in evidence Clone's 1986 Federal income tax returns. The returns show that Clone reported Federal gross receipts for the period April 1, 1984 through March 31, 1987 of \$338,418.00. For the period in issue, June 1, 1984 through August 31, 1987, Clone reported taxable sales to the State of \$210,796.00. When asked about this discrepancy under cross-examination, Mr. Koenig explained that he did not begin reporting admission receipts as taxable sales until sometime after the prior audit concluded. Mr. Filaski testified that he did not know when Clone began charging an admission. The prior audit found that Clone did charge an admission when it was operating Feathers.

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error until preparing for the administrative hearing.

We modified finding of fact "8" to accurately reflect the record.

Petitioners offered in evidence a set of register tapes collected by Bruce Filaski during the audit period. These consisted of five bundles of envelopes covering the period August 1984 through November 1985 and a sixth bundle covering the period March 1, 1986 through May 31, 1988. These records indicate that Feathers stopped serving alcoholic beverages on December 28, 1986 and began doing business strictly as a teen disco after that date. By and large the envelopes are dated, but there is no consistency in how the tapes were maintained. For instance, some envelopes purport to contain tapes for a single day while others purport to contain tapes for a three-month period. The envelopes tend to show that Feathers did business on Friday, Saturday and Sunday nights. Two of the bundles have totals shown on the front which reconcile to reported taxable sales for corresponding periods. The other bundles were submitted without a summary. On their face, the envelopes which correspond to the period in which Clone was operating Feathers do not indicate whether admission receipts are included in the recorded figures.

The cash register tapes are of no use for purposes of determining Clone's taxable sales for the audit period. Neither Bruce Filaski nor Mr. Koenig could offer any information regarding Clone's recordkeeping procedures. Mr. Filaski stated that the cash register tapes were used as a basis for reporting sales, but he offered no worksheets, journals, ledgers or other documents which would enable one to reconcile the tapes to reported taxable sales. Furthermore, he was unable to answer any questions with regard to figures shown on the tapes.

Mr. Koenig prepared Clone's sales tax returns. He did not use the cash register tapes to do so (in fact, he testified that he never saw the tapes until the day of the hearing); rather, he reported taxable sales in an amount verbally provided to him by Mr. Filaski. Mr. Koenig reconciled Clone's checkbook and reviewed its bank statements. He prepared Clone's Federal income tax returns using his summaries of those records. The records relied on by Mr. Koenig to prepare the Federal returns were not placed in evidence.

Petitioner Bruce Filaski, William Filaski and Bradley Filaski conceded being persons responsible for collection of, reporting and paying over sales tax on behalf of Clone.

***OPINION***

The Administrative Law Judge determined that since petitioners made no books and records available to the Division despite repeated requests for them, the Division had the right to estimate taxes due from petitioners based on external indices. Further, the Administrative Law Judge found that, in view of petitioners' "studied disregard of the Division's repeated messages and persistent attempts to schedule an audit appointment," the Division acted reasonably in refusing to postpone the audit any further (Determination, p. 10).

Finding petitioners' cash register tapes -- the only proof of actual sales submitted -- to be unacceptable, the Administrative Law Judge concluded that petitioners had presented no evidence that the observation test was inaccurate or erroneous in any way. Despite this, the Administrative Law Judge disapproved of the way in which the Division used the observation test results to estimate total sales for the audit period. Specifically, because she found that the disco was opened only three nights per week, the Administrative Law Judge found irrational the Division's decision to compute taxable sales for the audit period by multiplying by seven the average daily sales figure derived from the observation of the disco, to compensate for what the Administrative Law Judge termed the "items extrinsic to the observation test," namely, the sales from catering, private parties hosted throughout the audit period, and alcoholic beverages served at the club while it was an adult disco (Determination, p. 13). Because no evidence of the extent of sales associated with such activities was introduced, and the Administrative Law Judge was not satisfied that the Division had offered any reason for the assumption that such activities amounted to four times daily receipts, the Administrative Law Judge cancelled 4/7 of the assessment corresponding to this estimate, and ordered the Division to recalculate the notices based on weekly taxable sales of three times the average daily sales figure used.

On exception, while the Division maintains that the method of computation used was both warranted and reasonable, the Division seems to accept the Administrative Law Judge's



conclusion that the notices of determination be modified. However, the Division requests that at most the assessment be reduced by 3/7 rather than 4/7, as petitioners' business operated at least four times per week throughout the audit period. In the alternative, the Division asserts that even if the Tribunal does not find that the disco was open four days per week, the assessment should, nevertheless, be calculated on a four-day per week basis to account for the sales of alcohol, the private parties hosted, and the catering done during the audit period. Additionally, the Division asks that the notices be adjusted to correct for the Division's error in calculating the discount on admission fees for Saturday nights.<sup>3</sup>

Petitioners submitted no brief in response, but concentrated below on their claim that the audit should have been postponed until their accountant came to New York. The Administrative Law Judge noted that while petitioners did not specifically so argue, they apparently believed the cash register tapes offered to be accurate, adequate representations of taxable sales during the audit period.

We modify the determination of the Administrative Law Judge.

First, we deal with the Division's primary request that the assessment be reduced by 3/7 rather than 4/7, to account for the four days per week that the disco was in operation during the audit period. As we conclude the record supports a finding that the disco was open four days per week, and have so indicated in our additional finding of fact, we hereby grant the Division's request and order the Division to modify the notices in accordance with this decision.

We turn now to the Division's second request, namely, that we adjust the notices to correct the Division's error in calculating the discount on admissions prices on Saturday nights. The result of the Division's error is that the average daily receipts figure,<sup>4</sup> that was used as the basis for calculating the total assessment, was \$52.00 less than it should have been (receipts of \$2,720.00 from the Wednesday night observation were averaged with estimated Saturday night

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<sup>3</sup>As noted above, the auditors believed that a "V.I.P." discount card entitled the holder to a \$2.00 reduction on entrance fees on Saturday nights, rather than the \$1.00 reduction the card actually allowed. This mistake caused an undercount in Saturday night admissions of \$104.00, for a total of \$1,416.00 instead of \$1,520.00

<sup>4</sup>The word "receipts" in this paragraph refers to the total of admissions plus soda sales.

receipts of \$1,560.00, instead of \$1,664.00, for an average of \$2,140.00, instead of \$2,192.00, a \$52.00 difference). This \$52.00 difference becomes significant when it is multiplied by the four days per week which we conclude the disco was in operation throughout the audit period ( $\$52.00 \times 4 = \$208.00 \times 13$  weeks per quarterly period = \$2,704.00). In view of the fact that we are reducing the notices by 3/7 from the amount originally assessed against petitioners, our grant of the Division's request to correct the error in calculating admission fees still results in a reduction in petitioners' assessment and is, thus, a permissible recalculation under sections 1138(a)(1) and 1138(a)(3)(B) of the Tax Law. Accordingly, we grant the Division's request to correct the error made.

Our decision in this matter renders further discussion of the issue unnecessary.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is granted;
2. The determination of the Administrative Law Judge is modified, to the extent that the average daily sales figure used in computing the assessment is adjusted to correct for the error made in the calculation of admission fees, and the total assessment is recalculated based on a four-day week;
3. The petitions of Clone Enterprises, Inc., Bruce Filaski, Bradley Filaski and William Filaski as officers of Clone Enterprises, Inc. are granted to the extent that the assessment is recalculated based on a four-day week, but are otherwise denied; and

4. The Division of Taxation is directed to recalculate the notices of determination dated September 10, 1987 and December 20, 1987 in accordance with paragraph "2" above, but the notices are otherwise sustained.

DATED: Troy, New York  
March 19, 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