STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
PETAK'S OF NEW YORK, INC. AND ROBERT PETAK, AS OFFICER	:	DECISION DTA No. 807506
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 May 31, 1987.	:	

Petitioners Petak's of New York, Inc. and Robert Petak, as Officer, 1224 B Madison Avenue, New York, New York 10128, filed an exception to the determination of the Administrative Law Judge issued on February 18, 1993. Petitioners appeared by Isaac Sternheim & Co. (Isaac Sternheim, C.P.A.). The Division of Taxation appeared by William F. Collins, Esq. (Michael B. Infantino, Esq., of counsel).

Both parties filed briefs on exception. Petitioners' request for oral argument was denied. The six-month period to issue this decision began on May 6, 1993, the date by which petitioner could have submitted a reply brief.

Commissioner Dugan delivered the decision of the Tax Appeals Tribunal. Commissioner Koenig concurs.

ISSUES

I. Whether the notices of determination issued to petitioners were issued by the City of New York rather than by the State of New York and were, therefore, invalid.

II. Whether the Administrative Law Judge erred in determining that the validity of the original audit was an issue in this case.

III. Whether the audit method employed by the Division of Taxation was reasonably calculated to reflect tax due and, if so, whether the results obtained therefrom have been shown by petitioners to be erroneous.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for findings of fact "5" and "6" which have been modified. The Administrative Law Judge's findings of fact and the modified findings of fact are set forth below.

Pursuant to an audit of Petak's of New York, Inc. ("Petak's") which commenced in July 1987, the Division of Taxation ("Division"), on June 20, 1988, issued two notices of determination and demands for payment of sales and use taxes due to Petak's as follows:

Period	Tax	Penalty	Interest	Total
6/1/84 - 5/31/87	$491,607.59	$129,920.44	$146,388.69	$767,916.72
9/1/85 - 5/31/87	$ 35,165.74	$ 35,164.75[1]		

On the same date, the Division also issued two notices of determination to Robert Petak, as officer of Petak's, assessing identical amounts for the same periods.[2]

Previously, on August 11, 1987, petitioner Robert Petak executed a consent on behalf of Petak's extending the period of limitation for assessment of sales and use taxes for the period June 1, 1984 through February 28, 1985 whereby it was agreed that such taxes for this period could be assessed at any time on or before June 20, 1988.

Each of the notices of determination issued to petitioners contained the following statements, printed in bold-faced type:

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[1] This notice of determination assessed "omnibus penalty" pursuant to Tax Law § 1145(a)(1)(vi).

[2] It should be noted that while the notices of determination were issued to Robert Petaks, based upon the power of attorney and consent signed by this petitioner, his correct name was Robert Petak.

> "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."

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

On the top of each of the notices of determination appeared "New York State Department of Taxation and Finance". In addition, petitioners were directed to make payment to "N.Y.S. Sales Tax" at the New York office.

Petak's is a deli/gourmet store located at 1244 B Madison Avenue in New York City. There were no tables on premises. On July 28, 1987, an appointment letter was sent, by certified mail, to Petak's which, in addition to setting forth a proposed date of August 14, 1987 for the commencement of the audit, stated as follows:

> "All books and records pertaining to your Sales Tax liability for the period under audit should be available. This would include journals, ledgers, sales invoices, purchase invoices, cash register tapes, exemption certificates, etc. and all Sales Tax records. Additional information may be required during the course of the audit."

The period under audit, as set forth on the letter, was June 1, 1984 through May 31, 1987, the period at issue herein.

On August 7, 1987, the auditor (Ahmed Shehata) and his team leader (Richard Gudanek) visited the premises. They observed the sale of soda, beer, non-alcoholic wine and champagne and "a lot of sandwiches". Menus were also obtained.

On August 10, 1987, the auditor went to the office of Petak's accountant. A waiver was presented (the waiver was subsequently signed by Mr. Petak). On August 17, 1987, the auditor received a telephone call from the accountant advising that he no longer represented Petak's.

Petitioner Robert Petak thereupon informed the auditor that he was looking for a new representative and that he would let the auditor know when he had retained the new representative. The auditor requested books and records from Mr. Petak, but was furnished with none.

On November 20, 1987, the auditor sent (by certified mail) letters to Petak's and to petitioner Robert Petak. The letter stated, in part, as follows:

> "Please provide us with the following records for the audit period 6/1/84 to 5/31/87.
>
> 1. Cash receipts journal, depreciation schedules.
> 2. Disbursement journal.
> 3. Guest checks, cash register tapes.
> 4. Purchases journal.
> 5. General ledger.
> 6. Sales and purchase book.
> 7. All the sales tax returns with work sheets.
> 8. Federal, State and City Income Tax returns for three years under audit."

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

> The field audit report indicates that, in addition to the field visit made on August 7, 1987, the auditor and his team leader made additional visits to the business on November 20, 1987, November 27, 1987 and April 6, 1988.[3] During these visits, the auditor observed, among other things, a blackboard listing daily lunch specials, coffee and donut sales and sales of sandwiches and platters.
>
> Despite numerous requests for books and records, the auditor was informed that Mr. Petak was attempting to obtain the services of another accountant and that he would contact the auditor when that was accomplished. Books and records were never furnished to the auditor from the initial request (the letter of July 28, 1987) through the date of the issuance of the assessments (June 20, 1988).
>
> Petitioner Robert Petak testified that records requested were not available and that, while he used cash registers, the tapes were thrown out at the end of each day (see, Tr., pp. 174-177). The following colloquy between the Administrative Law Judge and petitioner occurred at the hearing:
>
> "ALJ FRIEDMAN: But in keeping your own books and records, how did you account for sales, taxable sales, and so forth?
>
> "THE WITNESS: I guess it was, you know, like any so-called mom-and-pop operation. We would just jot it down on pieces of paper and accumulate it and quarterly pay what added up. So-called cigar-box theory.

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[3] Due to an accident suffered by the original auditor, another auditor, M. Ramsubhag, wrote the audit comments and processed the case. He did not, however, take part in the audit while it was being performed.

"ALJ FRIEDMAN: At the end of a given day would you check the register to determine how much the receipts were?

"THE WITNESS: We would balance the registers, yes. And we would mark down what the taxable amount that was required to, you know, from that day, and then pay a quarter.

"ALJ FRIEDMAN: Then you had no source documentation to back up what you were reporting as taxable sales or nontaxable sales?

"THE WITNESS: As such, official ledgers, no, we did not. But if I may clarify something, the receipt that these gentlemen are talking about are not the end-of-day

receipts from the register, the tallies; are they? You're talking about a receipt from this $292?" (Tr., pp. 177-178).[4]

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

On its sales tax returns filed for the audit period, Petak's had reported approximately 1.4 percent of its gross sales as having been subject to tax. The auditor, his team leader and the unit head (Jan Goldberg) all agreed that, based upon their experience in auditing other delis and gourmet shops, this taxable percentage was extremely low.

Gross sales were accepted as filed. The auditor (Mr. Shehata), his team leader (Mr. Gudanek) and the branch chief (Noah Daniel) reviewed the menus obtained. The menus showed both taxable and nontaxable items offered for sale by petitioners. Included in the review were party menus, i.e., catering of prepared foods by petitioners.

According to Mr. Gudanek (Mr. Shehata was not available to testify) who testified at the hearing, a review of the menus and an observation of the business revealed the sale of both taxable and nontaxable items and, under the circumstances (no books and records), they felt that a nontaxable percentage of 15 percent was reasonable. Mr. Gudanek also stated that while, under Tax Law § 1132(c), all nontaxable sales could have been disallowed absent books and records, to do so would not have been reasonable since it was obvious, from the visits to the business, that sales of nontaxable items were, in fact, being made. The assessments, as issued, were therefore computed by multiplying gross sales (as reported) by 85 percent, allowing for taxable sales reported and taxing adjusted taxable sales by the applicable rate (8.25 percent). Due to substantial underreporting and failure to maintain books and records, penalty was assessed. For the period

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[4] We modified this fact by adding the colloquy between the Administrative Law Judge and the witness to indicate clearly the reasons why petitioners did not furnish books and records to the Division and to amplify the recordkeeping method of petitioners.

> September 1, 1985 through May 31, 1987, omnibus penalty was also assessed on a separate notice of determination issued to each petitioner, since an amount in excess of 25 percent of the amount required to be shown on the returns had been omitted.[5]

A conciliation conference was held by the Bureau of Conciliation and Mediation Services on December 13, 1988. Petitioners appeared by Isaac Sternheim, C.P.A. and Jacob Herskovits, practitioner. The Division was represented by Messrs. Goldberg, Gudanek and Shehata. Mr. Gudanek stated that some records were shown to the conciliation conferee, but none were shown to the auditors.

Mr. Gudanek testified that the conciliation conferee wanted to cancel the assessment on the basis that a 15 percent nontaxable percentage was not reasonable, but he apparently was overruled by his superiors. Instead, the conferee directed the auditors to perform an observation test. Petitioners' representative agreed to provide access to the business premises for purposes of performing the observation test, but he did not agree to be bound by its results.

On March 14, 1989, the observation test was performed at Petak's during the hours of 7:00 A.M. to 8:00 P.M. Mr. Gudanek, Mr. Shehata and various other auditors performed the test (Mr. Herskovits, on behalf of petitioners, was present during a portion of the observation).

During the observation test, two cash registers were being used (there were two other registers in the back of the store). There was a microwave oven which the auditors were informed was out of order; however, during the afternoon, one of the employees used it to heat something for his personal consumption. Mr. Gudanek stated that, while catering orders did go out, they were slow on that day. At about 6:15 P.M., a catering order for several hundred dollars went out, but the auditors were not allowed to see its contents. On one other order, the

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[5] In view of the finding of fact that petitioner did not maintain books and records, we eliminate, as irrelevant, the following sentence from this fact:

> "Mr. Gudanek testified that the taxpayer stated, on a number of occasions, that complete books and records were maintained, so use of an observation test was not possible."

auditors did not see the entire contents although they observed roast chicken on the top. They requested the cash register tapes for the day, but Mr. Petak gave them only the final totals.

Pursuant to the observation test, gross sales for the day were $8,243.93. Taxable sales were $2,639.44. The resulting taxable percentage was 32.0187 percent. Applying this percentage to gross sales resulted in taxable sales, for the audit period, of $2,283,235.10 which, when taxed at the applicable rate, resulted in total tax due of $188,366.91. Credit for tax paid ($8,480.90) reduced total tax due to $179,886.01, plus penalty and interest.

On October 6, 1989, a conciliation order was issued which reduced the assessments issued to each petitioner from $491,607.59 to $179,886.01, plus penalty and interest. In addition, the order reduced the omnibus penalty, assessed against each petitioner, from $35,165.74 to $12,797.15.

At the first hearing (October 15, 1991), Mr. Gudanek stated that his office (New York City Department of Finance - Sales Tax Unit), more particularly Mr. Shehata, prepared the assessments, had them typed in the office by a typist and mailed them to petitioners. Since the Division objected, at the hearing, to the raising of this jurisdictional issue (the lack of authority of the City Department of Finance to issue assessments) which was raised neither in the petition nor at the outset of the hearing, the Administrative Law Judge agreed to keep the record open to allow rebuttal evidence. At the hearing held on April 30, 1992, Joseph Maccio, Sales Tax Auditor II, appeared and testified as to his involvement with the assessments at issue.

In 1988 (when the assessments were issued), Mr. Maccio was the State liaison to the Metropolitan Audit Group of the New York City Department of Finance. His function was to oversee the City operation to ensure that the Division's procedures and policies were followed. Among his other duties were to review audit cases and monitor informal protest cases.
Mr. Maccio testified that, with respect to the present matter, he discussed it with Noah Daniel and Jan Goldberg of the Metropolitan Audit Group who explained to him the facts and circumstances (more particularly, the audit method employed). He stated that, after these discussions, he approved the mailing of the assessments by the Metropolitan Audit Group.

The Division introduced into evidence a copy of an agreement, dated September 13, 1971 (as well as amendments and subsequent agreements) between the former State Tax Commission and the Finance Administrator of the City of New York with respect to the administration of sales and use taxes imposed by the State pursuant to Article 28 of the Tax Law and by the City pursuant to the authority of Article 29 of the Tax Law. These agreements, necessitated by chapter 771 of the Laws of 1971 (amending Tax Law § 1142), provided for the delegation to the Finance Administrator and his employees and agents the power to examine the books and records of persons in the City of New York who are subject to sales and use taxes pursuant to Article 28 of the Tax Law, subject to certain limitations. One such limitation was that no power was delegated with respect to review, assessment, appeal or any other or further action other than the power to conduct examinations.

At the second hearing (April 30, 1992), Mr. Gudanek stated that the Metropolitan Audit Group did not issue the assessments, but merely mailed them with the permission of the State.

Petitioner Robert Petak testified that this corporation was formed in August 1983 and that the business opened on April 4, 1984. Petitioner and Richard Petak were the sole officers and shareholders. Another corporation (same principals) operates a Petak's on Pearl Street in New York City. Petitioner stated that each Petak's has separate menus and that the store at issue (Madison Avenue) has a less extensive menu because it was primarily involved in retail sales. Mr. Gudanek testified that all of the menus which he and the other personnel reviewed were obtained at the Madison Avenue store, yet the menus contained the addresses of both locations. All but one of the menus (Exhibit "H") do, in fact, contain both the Pearl Street and Madison Avenue addresses.

Petitioner Robert Petak testified that there was no salad bar at Petak's until at least November 1988 at which time a salad bar refrigerator was purchased. In furtherance thereof, the invoice relative to the purchase of this salad bar refrigerator (the invoice was dated November 3, 1988) was introduced into evidence (Exhibit "2"). While Mr. Gudanek testified that there was a salad bar at the time that the observation test was performed (March 14, 1989),

he could not recall whether or not he observed a salad bar during any of his four visits prior to the issuance of the assessments. From the audit workpapers, it appears that, out of total daily sales for the day of the observation, $237.13 represented taxable salad bar sales.

Mr. Petak stated that register tapes were not kept, but were disposed of at the close of business each day. He denied refusing, during the course of the observation test, to allow the auditors to view the contents of any of the take-out orders or to give the cash register tapes to the auditors at the close of business on that day.

OPINION

The Administrative Law Judge rejected petitioners' assertion that the notices of determination were invalid because they were issued by the City of New York rather than New York State. Relying on our decision in Matter of Malson, Ltd. (Tax Appeals Tribunal, September 12, 1991), the Administrative Law Judge concluded that:

> "the fact that the notices of determination indicate that they were issued by New York State coupled with the Division's agreement with the City Department of Finance and Mr. Maccio's [the audit team leader] testimony that he approved the mailing of the notices clearly indicate that it was New York State, not the City Department of Finance, which issued these assessments and, as such, petitioners' contention that they should be cancelled because they were violative of Tax Law § 1142(10) must be rejected" (Determination, conclusion of law "B").

The Administrative Law Judge next determined that:

> "it is the original audit method and the resulting assessments which, if shown by clear and convincing evidence to be erroneous, would warrant cancellation thereof even if it were to be found that the post-assessment audit method (the observation test) and the reduced assessments were reasonable. A statutory notice cannot be sustained on the basis of information gathered after the notice was issued, even if that information establishes that the amount of tax assessed by the statutory notice was reasonable (see, Matter of Roncone, State Tax Commission, March 11, 1986 [TSB-H-86(83)S])" (Determination, conclusion of law "C").

With regard to the original audit, the Administrative Law Judge concluded that the Division properly requested books and records from petitioners and that no records were provided by petitioners. The Administrative Law Judge found that:

> "at no time did petitioners produce any evidence to show that this [15%] was unreasonable. They merely asserted that an estimate based upon

> audit experience, review of menus and observation of the business was, patently, unreasonable. [Accordingly] . . . it must be determined . . . that . . . petitioners have failed to establish, by clear and convincing evidence, that the method and the resulting assessment were erroneous" (Determination, conclusion of law "C").

Finally, the Administrative Law Judge determined that petitioners proved that they did not have salad bar sales during the audit period and adjusted the assessment accordingly.

On exception, petitioners assert that the assessment was issued by the City of New York in violation of Tax Law § 1142(10) and was, therefore, invalid.

Petitioners also assert that the Administrative Law Judge erred in dealing with the original audit since "[t]he Conciliation Conferee . . . determined that the assessment was issued without any rational basis and was of the opinion that the assessment should be cancelled . . ." (Petitioners' memorandum in support of exception). Petitioners assert that they established that the audit method was clearly erroneous and not reasonably calculated to estimate petitioners' tax liability, in that, contrary to the determination of the Administrative Law Judge, it was not based on auditor experience with similar establishments or on an observation of petitioners' business activity; rather, the taxable ratio was "arrived at via a 'meeting of minds'. . . not supported by any computations, documentation or proof at all" (Petitioners' memorandum in support of exception).

Petitioners go on to assert that "[t]he issue at the hearing [concerning audit methodology] was not whether the original (85% taxable ratio) basis was a valid one but rather whether the revised assessment [resulting from the Conciliation Conference] based entirely on information garnered after the assessment had been issued should be sustained" (Petitioners' memorandum in support of exception, emphasis in original). Petitioners assert that: "it is quite clear from the evidence and from the testimony that the 32% taxable ratio was developed from an observation test performed long after the fact and cannot be used as a basis . . ." (Petitioners' memorandum in support of exception).

The Division, in response to the exception and citing our decision in Matter of Sandrich, Inc. (Tax Appeals Tribunal, April 15, 1993), issued after the determination in this matter, supports the conclusion of the Administrative Law Judge that the validity of the original audit is the proper issue, not the validity of the revision to the assessment resulting from proceedings before the Bureau of Mediation and Conciliation. The Division urges that the determination of the Administrative Law Judge be affirmed in its entirety and the Notice of Exception dismissed.

We affirm the determination of the Administrative Law Judge.

We deal first with petitioners' assertion that the Notice is invalid because it was issued by the City of New York in violation of section 1142(10) of the Tax Law.[6] This issue was fully and correctly dealt with by the Administrative Law Judge in his determination and, for the reasons stated therein, we affirm.

We deal next with petitioners' assertions that the issue at hearing was not the validity of the original audit method, but whether the revised assessment based on information garnered after the assessment was issued should be sustained. We affirm the determination of the Administrative Law Judge based on our decision in Matter of Sandrich, Inc. (supra) where we stated:

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[6]Tax Law § 1142(10) authorizes the Commissioner of the State Department of Taxation and Finance:

> "[t]o delegate from time to time and in whole or in part, when it deems it to be in the best interests of the state, to the commissioner of finance of the city of New York and his employees and agents, and to the county executives of Nassau and Suffolk counties and their employees and agents its power to examine the books and records of any person in the city of New York or the counties of Nassau and Suffolk who is subject to the taxes imposed by or required to file returns pursuant to this article; provided, however, that (a) such delegation shall relate solely to examining books and records and not to review, assessment, appeal, or any other action taken on the basis of such examination, (b) every examination made pursuant to such delegation shall be conducted in accordance with the direction, methods, rules, practices, procedures, and regulations of the commissioner of taxation and finance, (c) no power shall be delegated to re-examine books and records for periods previously examined by the commissioner of taxation and finance, his agents or employees, and (d) such delegation shall limit the county executives of Nassau and Suffolk counties to examine only those books and records of persons within their respective counties."

> "[t]he Bureau of Conciliation and Mediation Services is established within the Division [of Taxation] and is responsible 'for providing conciliation conferences' (Tax Law § 170[3-a][a]). Such conferences are provided at the sole option of the taxpayer.
>
> "Petitioners here elected to petition for a hearing in the Division of Tax Appeals. As a result, petitioners, at hearing, could not rely in any way on the prior proceedings since the conciliation order cannot 'be considered as precedent or be given any force or effect in any subsequent administrative proceeding' with respect to petitioners (Tax Law § 170[3-a][f]). We agree with the Division that because of this statutory language, there was no authority for the Administrative Law Judge to consider the validity of the methodology used in proceedings at the Bureau of Conciliation and Mediation Services and to substitute his own methodology for that of the conferee. To the extent that our decision in Matter of Commack Fish & Seafood Rest. Corp. (Tax Appeals Tribunal, March 12, 1992) implies that an Administrative Law Judge may delve into the substance of the conciliation proceedings, it is hereby overruled" (Matter of Sandrich, Inc., supra).

We also point out that petitioners viewed the validity of the initial audit as an important issue since they challenged such in their petition, i.e., "[t]he original assessment had no rational foundation and was therefore reduced at a Conciliation Conference" (Petitioner's petition) and spent considerable time at hearing cross-examining the Division's witness on the methodology of the initial audit (see, Tr., pp. 43-110).

We deal next with the validity of the original audit method. The rubric for the conduct of sales tax audits is that:

> "[b]ecause the statutory authority to determine a taxpayer's sales tax liability by estimate procedures rests upon a finding that the taxpayer's books and records are inadequate to conduct a complete audit, the Division is required to first request (Matter of Christ Cella v. State Tax Commn., 102 AD2d 352, 477 NYS2d 858, 859) and thoroughly examine (Matter of King Crab Rest. v. Chu, 134 AD2d 51, 522 NYS2d 978, 979-980) the taxpayer's books and records for the entire period of the proposed assessment (Matter of Adamides v. Chu, 134 AD2d 776, 521 NYS2d 826, 828, lv denied 71 NY2d 806, 530 NYS2d 109), in order to determine from verification drawn independently from within these records whether they are sufficient to support a complete audit (Matter of Meyer v. State Tax Commn., 61 AD2d 223, 402 NYS2d 74, 76, lv denied 44 NY2d 645, 406 NYS2d 1025). If the Division's examination establishes that the taxpayer's records are adequate and complete, the taxpayer is entitled to have its assessment calculated based upon a detailed audit of those records (Matter of Kennedy & Co. v. Chu, 125 AD2d 773, 509 NYS2d 199; Matter of Allied New York Servs. v. Tully, 83 AD2d 727, 442 NYS2d 624; Names in the News v. New York State Tax Commn., 75 AD2d 145, 429 NYS2d 755; Matter of Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 411 NYS2d 41)"

(Matter of Marine Midland Bank, Tax Appeals Tribunal, May 13, 1993).

Here, the Division made a proper request for books and records. No records were produced by petitioners because, by petitioners' own testimony, none existed. Accordingly, the Division, pursuant to Tax Law § 1138(1), was authorized to estimate petitioners' tax liability. The Division accepted petitioners' gross sales as reported on their returns. The salient issue was the correctness of petitioners' assertion that 98.4% of these sales were not taxable. In view of the fact that petitioners were in the deli/gourmet business, the auditors acknowledged that petitioners made some sales which were not taxable and, thus, that there should be some allowance for such sales (see, Matter of Bernstein-on-Essex St., Tax Appeals Tribunal, December 3, 1992; cf., Matter of Savemart, Inc. v. State Tax Commn., 105 AD2d 1001, 482 NYS2d 150, appeal dismissed 64 NY2d 1039, 489 NYS2d 1029; Matter of Academy Beer Distribs., Tax Appeals Tribunal, January 21, 1993 [in the absence of books and records, the Division is entitled to rely on the presumption of taxability in Tax Law § 1132(c)]).

The dilemma for the Division was how to determine just what percentage of petitioners' gross sales was not taxable since petitioners offered no books and records whatsoever to provide the Division with a basis to make such a calculation.

We agree with the Administrative Law Judge that petitioners have not met their burden of showing that the audit methodology chosen by the Division was not reasonably calculated to estimate petitioners' nontaxable sales and that the amount of the assessment is erroneous (Matter of Surface Line Operators Fraternal Org. v. Tully, 85 AD2d 858, 446 NYS2d 451).

Petitioners cannot meet their obligation to prove by clear and convincing evidence that the result of the method was unreasonable, inaccurate or that the amount of the tax assessed is erroneous merely by arguing a different method for estimating tax liability, even if the proposed alternative method has merit (see, Matter of Meskouris Bros. v. Chu, 139 AD2d 813, 526 NYS2d 679, 681, citing Matter of Surface Line Operators Fraternal Org. v. Tully, supra, 446 NYS2d 451, 453; see also, Matter of Club Marakesh v. Tax Commn. of the State of New York, 151 AD2d 908, 542 NYS2d 881, lv denied 74 NY2d 616, 550 NYS2d 276). The Division is

not required to pick the most accurate audit method, but merely a rationally based one (see, Matter of Grecian Sq. v. New York State Tax Commn., 119 AD2d 948, 501 NYS2d 219, 221). Furthermore, exactitude is not required when the need to resort to estimating tax liability is due to the taxpayer's own failure to keep adequate records (see, Matter of Grant Co. v. Joseph, 2 NY2d 196, 159 NYS2d 150, 157, cert denied 355 US 869; Matter of Markowitz v. State Tax Commn., 54 AD2d 1023, 388 NYS2d 176, 177, affd 44 NY2d 684, 405 NYS2d 454).

The record establishes that the Division's estimate of nontaxable sales was based on a review of petitioners' menus, the observations of petitioners' business from the several visits made by the auditor, and the experience of the auditor, the team leader and the unit head with auditing similar type establishments. We find this use of audit experience in conjunction with on-site observation and review of menus, a reasonable basis for estimating petitioners' nontaxable sales (see, Matter of Hanratty's/732 Amsterdam Tavern v. New York State Tax Commn., 88 AD2d 1028, 451 NYS2d 900, appeal dismissed 57 NY2d 954, 457 NYS2d 1028 [audit method sustained where, based on past experience, and using the selling prices according to the taxpayer's menus and taxpayer's employees, the taxpayer's book markup percentages were determined to be too low]; Matter of Oak Beach Inn Corp. v. Wexler, 158 AD2d 785, 551 NYS2d 375 [sustaining audit method using markup percentage for food purchases based on experience with similar establishments]; Matter of Carmine Rest. v. State Tax Commn., 99 AD2d 581, 471 NYS2d 402 [sustaining auditor's conclusions on number and cost of meals served to employees based on auditor's experience and taxpayer's records]; cf., Matter of Grecian Sq. v. New York State Tax Commn., supra [insufficient evidence to sustain auditor's increase in sales figures based on experience with other establishments he had audited]; Matter of Basileo, Tax Appeals Tribunal, May 9, 1991 [where the basis of the assessment is a comparison to similar businesses, the Division must be able to respond meaningfully to inquiries concerning the other businesses in order for the audit to be sustained]). In short, the Division's witness, here, responded to all questions on cross-examination and adequately explained the methodology. Moreover, petitioners raised no issue of merit concerning the

experience of the members of the Division's audit staff. We conclude the method was reasonable. While it is true, as petitioners' assert, that the Division could have elected to perform an observation test of petitioners' business, which may have produced a better tax result for petitioners, the fact that the Division chose not to do so does not make the method chosen unreasonable.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Petak's of New York, Inc. and Robert Petak, as Officer, is denied;

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

3. The petition of Petak's of New York, Inc. and Robert Petak, as Officer, is granted to the extent indicated in conclusions of law "D" and "E" of the Administrative Law Judge's determination, but is otherwise denied; and

4. The Division of Taxation is directed to modify the notices of determination and demand for payment of sales and use taxes due dated June 20, 1988 in accordance with paragraph "3" above, but such notices, as modified by the Conciliation Order of October 6, 1989, are otherwise sustained.

DATED: Troy, New York
September 9, 1993

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

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