STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
PETAK'S OF NEW YORK, INC. AND ROBERT PETAK, AS OFFICER	:	DETERMINATION
		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 a petition 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.

A hearing was commenced before Brian L. Friedman, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York on October 15, 1991 at 1:15 P.M., and was continued to conclusion before the same Administrative Law Judge at the same location on April 30, 1992 at 9:15 A.M., with all briefs to be submitted by August 1, 1992. 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).

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 were, therefore, invalid.

II. 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.

III. Whether, based upon the books and records provided to the auditor, 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

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 boldfaced 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."

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

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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.

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."

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).

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. 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 testified that the taxpayer stated, on a

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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.

number of occasions, that complete books and records were maintained, so use of an observation test was not possible. 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 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.

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 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.

SUMMARY OF PETITIONERS' POSITION

(a) An observation test could have been performed, initially. The auditors were not told there was a complete set of books and records.

(b) The initial assessment was based upon a total observation of 42 minutes combined with a cursory review of menus. No menu analysis (as to taxable versus nontaxable items) was performed.

(c) The observation test was performed only after the conciliation conferee indicated that he wanted to cancel the assessment due to the fact that the 15 percent nontaxable percentage was not reasonable. Since the original assessment was unreasonable, it cannot thereafter be validated by the use of another audit method.

(d) With respect to the results of the post-assessment observation test, there are the following errors:

(1) During the audit period, there was no salad bar. Salad bar sales, made during the observation test, were used to determine the taxable percentage.

(2) Chicken was not sold in a heated state and was, therefore, nontaxable. Petak's did not have a heating lamp.

(3) Salads sold with sandwiches were sold by the pound and were, therefore,

nontaxable. Sandwiches and salads were never put together on a platter.

(e) The notices of determination issued to petitioners were jurisdictionally defective because they failed to indicate that the tax assessed was estimated (the box was not checked).

(f) Contrary to statutory authority, the assessments were not issued by the State, but were actually issued by the City Finance Department and, as such, are invalid.

CONCLUSIONS OF LAW

A. Tax Law § 1138(a)(1) provides, in part, 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."

Tax Law § 1138(a)(2) provides:

> "Whenever 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 through a hearing process; and that the petition for such challenge must be filed with the tax commission within ninety days."

As indicated in Finding of Fact "3", the box which indicated that the assessment had been estimated was not checked on any of the notices of determination at issue.

In Matter of Negat, Inc. (Tax Appeals Tribunal, April 9, 1992) and in Matter of Cheakdkaipejchara (Tax Appeals Tribunal, April 23, 1992), the Tribunal reviewed the legislative history of Tax Law § 1138(a)(2). In Cheakdkaipejchara, the Tribunal stated:

> "We find nothing in this legislative history which supports the conclusion offered by petitioner and embraced by the Administrative Law Judge and dissent herein 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 as a matter of law. Indeed, we find such 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."

In Matter of Mon Paris Operating Corp. v. Commissioner of Taxation and Finance (Sup

Ct, Albany County, March 16, 1988, affd on other grounds 151 AD2d 822, 542 NYS2d 61), the court held that the failure, by the Division, to indicate that the tax was estimated did not invalidate the assessment. Instead, it held that the taxpayer must have been prejudiced by this omission in order to invalidate the notice. Since the petitioner was aware of the estimated nature of the tax and of his need to pursue a remedy, the court found that no prejudice existed.

In the present matter, books and records were requested from petitioners on numerous occasions, but none was ever furnished. Both from their petition and from the evidence presented at the hearing, it is clear that petitioners were aware that both the initial assessments and the reductions made in the conciliation order were based upon estimates. Since petitioners were not prejudiced, were fully apprised of the audit methods employed and timely pursued administrative remedies, the assessments issued to such petitioners must not be invalidated based upon the failure of the Division to indicate that the assessments were estimated.

B. Chapter 771 of the Laws of 1971 added a new provision to section 1142 of the Tax Law which granted to the former State Tax Commission the power to delegate certain examining and auditing functions to the Finance Administrator of the City of New (now Commissioner of Finance). This provision, Tax Law § 1142(10), which was renumbered from subdivision 9 to subdivision 10 by chapter 89 of the Laws of 1976 and amended to substitute Commissioner of Finance for Finance Administrator, provides as follows:

> "To 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, its power to examine the books and records of any person in the city of New York 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 commission, and (c) no power shall be delegated to re-examine books and records for periods previously examined by the commission, its agents or employees."

Pursuant to the above provision, the City of New York is permitted to conduct audits and to otherwise examine books and records of taxpayers in New York City who are subject to State sales and use taxes. However, the power to assess such taxes was not delegated and, therefore,

remains solely with the State.

As indicated in Finding of Fact "8", the Division offered into evidence a copy of certain agreements between the State and City to implement the provisions of Tax Law § 1142(10). In addition, Joseph Maccio testified that he met with the auditors' supervisors to discuss the specifics of this case and that he approved the mailing of the assessments by the Metropolitan Audit Group. In Matter of Malson, Ltd. (Tax Appeals Tribunal, September 12, 1991), the Tribunal stated:

> "We conclude that petitioners have not established that the instant notices were issued in a manner that violated section 1142(10) of the Tax Law. The notices themselves indicate that they were issued by New York State: there is no mention of New York City on the document . . . . The only evidence that petitioners can be relying on to support their position is the testimony of the auditor that the assessments were sent out by the auditor's office which was the Metro Group, City of New York under the direction of the State . . . . While the Division has elected not to explain the relationship between the City and the State with respect to the issuance of the instant notices (footnote omitted), we conclude that the fact that the auditor testified that the notices were mailed by the Metro Group office is not sufficient to establish that the notices were not issued by the State of New York."

In the present matter (as in Malson, supra), the team leader (Mr. Gudanek) testified that his office sent out the assessments after they completed the audit. However, 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 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.

C. Tax Law § 1135(a) provides that:

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

Tax Law § 1138(a)(1) provides, in part, that if a return required to be filed is incorrect or insufficient, the amount of tax due shall be determined on the basis of such information as may

be available. This section further provides that, if necessary, the tax may be estimated on the basis of external indices. The resort to external indices is predicated upon a finding of insufficiency in the taxpayer's recordkeeping such that verification of sales is a virtual impossibility (Matter of Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 411 NYS2d 41). In such circumstances, the Division must select a method of audit reasonably calculated to reflect tax due (Matter of Grecian Square v. State Tax Commn., 119 AD2d 948, 501 NYS2d 219), and the burden is on petitioner to establish by clear and convincing evidence that both the method used to arrive at the tax assessment and the assessment itself are erroneous (Matter of Sol Wahba, Inc. v. State Tax Commn., 127 AD2d 943, 512 NYS2d 542).

There is no dispute that books and records were requested and that none were provided by petitioners. Clearly, therefore, the Division's resort to external indices was proper.

Petitioners correctly contend that an observation test could have been performed initially. They maintain that the auditors were never informed that a complete set of books and records existed. Regardless of what was told to the auditors, books and records were never provided by petitioners. However, the auditors, in lieu of an observation test or other audit method, chose to estimate the percentage of Petak's taxable sales on the basis of audit experience, i.e., conducting audits of similar businesses in similar locations in conjunction with an examination of Petak's business operation and a review of its menus.

With respect to the observation test which was conducted subsequent to the issuance of the assessments (at the direction of the conciliation conferee), petitioners correctly point out 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]). Therefore, the original audit and the assessments derived

from that audit must be initially considered herein. Despite the fact that petitioners failed to maintain and/or produce adequate records, the reasonableness of the audit method must still be examined (see, Matter of House of Audio of Lynbrook, Tax Appeals Tribunal, January 2, 1992).

Mr. Gudanek testified that, despite the lack of books and records to substantiate an amount, it was clear, from a review of the menus and from an observation of the business, that Petak's made some nontaxable sales. Unlike Matter of Bernstein-on-Essex St. (Tax Appeals Tribunal, December 3, 1992), where, despite the fact that the petitioner was obviously making nontaxable sales, the auditor, citing Tax Law § 1132(c), deemed all sales to be taxable due to a lack of books and records, these auditors, relying on experience in auditing similar businesses in similar locations and on an observation of Petak's business, attempted to ascertain a reasonable nontaxable percentage. While it could be argued that there existed alternative audit methods which could have yielded more exacting results, "[w]here the taxpayer's own failure to maintain proper records prevents exactness in determination of sales tax liability, exactness is not required" (Matter of Meyer v. State Tax Commn., 61 AD2d 223, 402 NYS2d 74, 78, lv denied 44 NY2d 645, 406 NYS2d 1025; see also, Matter of Markowitz v. State Tax Commn., 54 AD2d 1023, 388 NYS2d 176, affd 44 NY2d 684, 405 NYS2d 454). 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).

In Matter of Top Shelf Deli (Tax Appeals Tribunal, February 6, 1992), the Tribunal stated as follows:

> "We also uphold as reasonable the auditor's assessment pertaining to petitioner's alleged catering services. The auditor's testimony that she had audited 50 similar delicatessens in the surrounding area provides a reasonable basis both for the five percent figure attributed to the catering, and the auditor's reliance on office experience (see, Matter of Convissar v. State Tax Commn., 69 AD2d 929, 415 NYS2d 305; cf., Matter of Grecian Sq. v. New York State Tax Commn., supra; Matter of Shop Rite Wines & Liqs., Tax Appeals Tribunal, February 22, 1991 [where the auditors failed to describe the office experience upon which they relied])."

While petitioners contend that the 15 percent nontaxable percentage (or, conversely, that

85 percent of its sales were taxable) was unreasonable, they have produced absolutely no books and records (other than their sales tax returns which indicated that approximately 1.4 percent of their sales were taxable) which would have permitted the auditors to calculate a potentially more accurate percentage.

In Matter of Atlantic & Hudson Ltd. Partnership (Tax Appeals Tribunal, January 30, 1992), the Tribunal concluded:

> "Although a determination of tax must have a rational basis in order to be sustained upon review (see, Matter of Grecian Sq. v. New York State Tax Commn., 119 AD2d 948, 501 NYS2d 219), the presumption of correctness raised by the issuance of the assessment, in itself, provides the rational basis, so long as no evidence is introduced challenging the assessment (see, Matter of Tavolacci v. State Tax Commn., 77 AD2d 759, 431 NYS2d 174; Matter of Leogrande, Tax Appeals Tribunal, July 18, 1991). Evidence that both rebuts the presumption of correctness and indicates the irrationality of the audit may appear: on the face of the audit as described by the Division through testimony or documentation (see, Matter of Snyder v. State Tax Commn., 114 AD2d 567, 494 NYS2d 183; Matter of Fortunato, Tax Appeals Tribunal, February 22, 1990); from factors underlying the audit which are developed by the petitioner at hearing (see, Matter of Ristorante Puglia, Ltd. v. Chu, 102 AD2d 348, 478 NYS2d 91; Matter of Fokos Lounge, Tax Appeals Tribunal, March 7, 1991 [where the petitioner proved that its utility meter readings bore no relationship to its level of business activity]; or in the inability of the Division to identify the bases of the audit methodology in response to questions posed at the hearing (see, Matter of Basileo, Tax Appeals Tribunal, May 9, 1991; Matter of Fokos Lounge, Tax Appeals Tribunal, March 7, 1991; Matter of Shop Rite Wines & Liqs., Tax Appeals Tribunal, February 22, 1991; Matter of Fashana, Tax Appeals Tribunal, September 21, 1989)."

At the hearing, petitioners' representative extensively questioned Mr. Gudanek about the procedures which led up to the arrival at the 15 percent nontaxable figure. However, at no time did petitioners produce any evidence to show that this percentage was unreasonable. They merely asserted that an estimate based upon audit experience, review of menus and observation of the business was, patently, unreasonable. As to the observation test performed subsequent to the issuance of the assessments, petitioners did offer testimony and/or documentation to challenge certain audit findings. These will be considered individually. But it must be determined, therefore, that, with respect to the original audit which gave rise to the assessments, petitioners have failed to establish, by clear and convincing evidence, that the method and the resulting assessment were erroneous.

D. Petitioners' objections to the results of the post-assessment observation test are set

forth in paragraph 10(d), supra.

As indicated in Finding of Fact "9", salad bar sales, for the day of the observation test, were in the amount of $237.13. Petitioner Robert Petak's testimony, coupled with the receipt for the purchase of a salad bar refrigerator in November 1988, substantiates that Petak's had no salad bar during the audit period. For purposes of the observation test, such sales should, therefore, be eliminated. Taxable sales per observation must be reduced from $2,639.44 to $2,402.31. Gross sales per observation must, accordingly, be reduced from $8,243.93 to $8,006.80. As a result thereof, the taxable percentage must be reduced from 32.0187 percent to 30.0034 percent.

Applying this revised percentage to gross sales for the audit period (Exhibit "F"; pg. 2 of audit workpapers) results in taxable sales being reduced from $2,283,235.10 to $2,139,658.87; additional tax due from $188,366.91 to $176,521.86; and, after credit for tax paid, total additional tax due from each petitioner is reduced from $179,886.01 (per Conciliation Order) to $168,040.96, plus penalty and interest. Omnibus penalty assessed against each petitioner must be reduced, accordingly.

As to petitioner Robert Petak's other contentions, i.e., that chicken was not sold in a heated state and that salads were not sold with sandwiches, his testimony, absent other corroborating evidence, cannot be judged to be more credible than the testimony and/or work product of the auditors who were on premises to conduct the observation test. Additional adjustments to the assessment cannot, therefore, be made herein.

E. The petition of Petak's of New York, Inc. and Robert Petak, as officer, is granted to the extent indicated in Conclusion of Law "D"; the Division is hereby directed to modify the notices of determination and demands for payment of sales and use taxes due issued to each petitioner on June 20, 1988, accordingly; and, except as so granted, the petition is in all other respects denied.

DATED: Troy, New York
February 18, 1993

/s/ Brian L. Friedman
ADMINISTRATIVE LAW JUDGE