

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
	:	
of	:	
	:	
592 SEVENTH AVENUE RESTAURANT, INC.	:	DECISION
	:	
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period June 1, 1979	:	
through May 31, 1982.	:	

Petitioner, 592 Seventh Avenue Restaurant, Inc., 592 Seventh Avenue, New York, New York 10036, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1979 through May 31, 1982 (File No. 41977).

A hearing was commenced before Doris E. Steinhardt, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on December 11, 1984 at 1:15 P.M. and was continued to conclusion on February 19, 1985 at 10:00 A.M., with all briefs to be submitted by June 30, 1985. Petitioner appeared by Lipsitz, Green, Fahringer, Roll, Schuller & James, Esqs. (Herald Price Fahringer, Esq., of counsel). The Audit Division appeared by John P. Dugan, Esq. (Irwin Levy, Esq., of counsel).

ISSUES

I. Whether the Audit Division was warranted in its resort to markup procedures to verify petitioner's sales of beer, wine and liquor.

II. If so, whether such markup procedures were erroneous for failure to consider, among other things: (1) the correct serving sizes of wine and liquor; (2) the inclusion in the selling prices of the sales tax; (3) the

maintenance on a daily basis of "happy hours"; and (4) employee and complimentary drinks.

FINDINGS OF FACT

1. On November 19, 1982, subsequent to the conduct of a field examination, the Audit Division issued to petitioner, 592 Seventh Avenue Restaurant, Inc., a Notice of Determination and Demand for Payment of Sales and Use Taxes Due, assessing sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1979 through May 31, 1982 in the amount of \$55,156.17, plus penalty and interest. On September 16, 1982, Stanley Malkin, as president of the corporation, had executed a consent to extend the period of limitations for assessment of sales and use taxes for the quarterly period ended August 31, 1979 to and including December 20, 1982.

2. Petitioner operates a topless bar, known as "The Golden Dollar," just off 42nd Street on Seventh Avenue in the Times Square area of New York City. The establishment is open for business 12:00 noon to 4:00 A.M. Monday through Saturday, and 4:00 P.M. to 4:00 A.M. on Sunday. Petitioner serves no food; its sales consist solely of wine, beer and liquor. It is undisputed that petitioner does not furnish its patrons with guest checks, and that the cash registers at the premises do not produce tapes. Daily receipts are deposited into the corporate account, and the documents pertaining to such account comprise the records of petitioner's sales.

3.(a) In April, 1982, the Audit Division commenced an examination of petitioner's records and operations. The sales tax examiner initially compared gross sales per petitioner's records with gross sales reported for federal corporation income tax purposes and for sales tax purposes and found these amounts to be in agreement. In view of the absence of cash register tapes and

guest checks, the Audit Division deemed petitioner's records inadequate and performed markup testing to verify petitioner's taxable sales.

(b) On Friday, April 30, 1982, at approximately 3:00 P.M., the examiner visited The Golden Dollar (with two other Audit Division representatives) and remained for approximately twenty to thirty minutes. There were very few patrons in the bar at that time. The examiner spoke with Mr. George Falack, petitioner's daytime manager, from whom he obtained the selling prices of drinks, a goblet in which wine is served to patrons, and a shot of liquor which the examiner transferred to a plastic vitamin container. Mr. Falack also informed the examiner that beer was sold by the 12-ounce bottle. Mr. Falack did not mention to the examiner employee theft, the provision of free drinks to employees, or the existence of a "happy hour", nor did the examiner make any inquiry concerning these matters.

(c) On the following Monday, at his office, the examiner determined the capacity of the wine goblet as $3\frac{1}{2}$ -ounces, using a one-ounce glass with $1/8$ -ounce demarcations. He washed and emptied the measuring device, transferred the liquor from the vitamin container to the device, and determined that the liquor serving size totalled $3/4$ of an ounce; the device was not dried prior to this procedure, apparently in an endeavor to account for any evaporation or spillage of the liquor.

(d) The examiner reviewed petitioner's cancelled checks for the period March 1, 1982 through May 31, 1982, which analysis disclosed beer purchases in the amount of \$5,632.75. Such amount represented 49.87 percent of petitioner's purchases of wine, liquor and beer for the quarterly period reviewed. By application of this percentage to petitioner's total purchases during the audit

period, the examiner calculated total beer purchases of \$59,355.00 and total wine and liquor purchases of \$59,663.00.

(e) The examiner calculated petitioner's markup percentages for beer and for wine and liquor as 869.12 percent and 1,271.02 percent, respectively. He determined petitioner's purchases of beer for the quarterly period ended May 31, 1982 by reference to paid bills. He estimated beer sales for such period by multiplying the total number of bottles purchased by the selling prices (\$3.25, \$3.50 or \$3.75 depending upon the brand name); he made no reduction to purchases to allow for such factors as breakage and spillage. The arithmetical steps of his beer markup calculation are shown below.

Sales \$54,588.00 - cost \$5,632.75 = profit \$48,955.25
Profit \$48,955.25/cost \$5,632.75 = beer markup 869.12%

The examiner's procedures in computing petitioner's markup of wine and liquor were similar, with the exception that he allowed a 15 percent reduction to purchases to account for spillage, breakage and buybacks. He estimated wine and liquor sales by multiplying the number of drinks per bottle (using serving sizes for wine and liquor of 3½-ounces and ¾ of an ounce, respectively) by the selling prices. His further steps are shown below.

Sales \$62,546.33 - cost \$4,562.03 = profit \$57,984.30
Profit \$57,984.30/cost \$4,562.03 = wine and liquor markup 1,271.02%

Finally, he marked up petitioner's beer purchases (\$59,355.00 x 869.12%) and wine and liquor purchases (\$59,663.00 x 1,271.02%) for the audit period, yielding audited taxable sales of \$1,393,212.00; he subtracted petitioner's reported taxable sales (\$710,127.00) from audited taxable sales to arrive at additional taxable sales, upon which tax of \$55,156.17 was due.

4. Petitioner points out that the examiner failed to follow the Department of Taxation and Finance sales and use tax guidelines for the bar and tavern industry in the following respects:

(a) he did not complete the bar questionnaire and bar fact sheet;

(b) he did not determine the number of employees, the rate of employee turnover and the reasons for employee discharge to judge the existence, if any, of employee theft;

(c) he failed to learn the vendor's policies regarding employee and complimentary drinks;

(d) he failed to inquire of the vendor about any allowance for a "happy hour"; and

(e) he did not inquire of the vendor whether the selling prices of drinks included the sales tax.

5. Throughout the audit period, petitioner served wine to its customers in goblets manufactured by Libbey Glass ("Rhine Wine" No. 8088); these glasses have a 4-ounce capacity. Throughout the audit period, petitioner served liquor in shot glasses manufactured by Anchor Hocking (No. 3667); these glasses have a capacity of 7/8 of an ounce. It was and is the practice of petitioner's bartenders to overpour servings of wine and liquor (to fill glasses to the brim so that a small amount of liquid spills over).

6. Throughout the audit period, the selling prices of all drinks served at The Golden Dollar were inclusive of sales tax, and signs to that effect were prominently displayed at the bar.

7. From 4:00 P.M. to 7:00 P.M. each day, petitioner maintains a "happy hour", during which customers may purchase two drinks for the price of one. The heaviest flow of customers occurs during these hours, in contrast with the

early afternoon (1:00 P.M. to 2:00 P.M.) and late evening (9:00 P.M. to midnight) when only a few customers are typically on the premises. Petitioner's accountant estimated that approximately 40 percent of the bar's business is transacted from 4:00 P.M. to 7:00 P.M.

8. Petitioner's employees regularly consumed and gave away drinks. Petitioner's accountant estimated that 3 percent of the sales computed by the examiner should properly be attributed to employee and complimentary drinks.

9. The examiner incorrectly considered Harvey's Bristol Cream a liquor. Harvey's Bristol Cream is a sherry and is served by petitioner in a 4-ounce goblet.

CONCLUSIONS OF LAW

A. That in the absence of the source documentation essential to verify petitioner's sales of beer, wine and liquor, the Audit Division was justified in its employment of markup tests. (Matter of Licata v. Chu, 64 N.Y.2d 873, revg., 105 A.D.2d 471.) Petitioner's position that given the nature of its business, adequate records consist of bank deposits of its cash proceeds is untenable. Records of bank deposits do not necessarily portray true sales and must themselves be subject to verification.

B. That petitioner established that the following adjustments to the markup testing are appropriate: (1) the serving sizes for liquor and for wine are to be augmented to 7/8 of an ounce and to 4 ounces, respectively; (2) all selling prices are to be decreased to reflect the inclusion therein of the sales tax; (3) audited sales are to be decreased by 20 percent (one-half of 40 percent) to account for the daily "happy hours"; and (4) Harvey's Bristol Cream is to be treated as a wine, sold in 4-ounce servings.

C. That the petition of 592 Seventh Avenue Restaurant Corp. is granted to the extent indicated in Conclusion of Law "B"; the Notice of Determination and Demand for Payment of Sales and Use Taxes Due issued on November 19, 1982 is to be reduced accordingly; and except as so granted, the petition is in all other respects denied.

DATED: Albany, New York

STATE TAX COMMISSION

AUG 21 1985

Roderick W. Cline
PRESIDENT

Francis J. Koenig
COMMISSIONER

Mark J. [Signature]
COMMISSIONER